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# The Urban-Rural Fringe Population Problem and Effects on Municipal Finance

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THE tremendous increase in the sub-urban population surrounding the majority of the larger cities in the United States gives rise to one of the key problems of municipal government finance today. This growth has resulted in the extension of the municipal economic area far beyond the existing political boundaries of many cities. The consequence of such extension of the economic area means that a large percentage of a city's working population may be nonresidents who commute daily from the suburbs or beyond to central city industries. The so-called daylight citizens use the central city's physical facilities such as streets, water, and police and fire protection, yet they contribute nothing directly to the costs of these necessary services in the form of tax payments. The burden of paying for these services necessarily rests on the residential and business population.

## Growth of Fringe Areas

Very little has been accomplished to overcome the effects of this rather serious urban-rural fringe population problem. It is growing more important annually. From 1940 to 1950 the sub-urban areas gained 9 million persons, or a 35 percent increase, compared with the central cities' gain of 5.7 million, or a 13 percent increase.<sup>1</sup> Sub-

urban growth in population was nearly two and one-half times that of the national rate of 14.5 percent, whereas the rate of central city growth fell somewhat short of the national average.

Part of this tremendous growth of the fringe area has resulted from an exodus of a large body of former residents of the central city to the suburbs in order to escape such undesirable features of the city as dirt, smoke, crime, slum areas, housing difficulties, and high property taxes. In many cases the artificial boundaries have not been altered to meet the desire of an increasing population to expand in normal fashion. One authority aptly compares the population flow beyond the artificial municipal boundaries to the taking off of hoops and barrel staves from a barrel of tar on a hot summer day.<sup>2</sup> In addition to this direct pressure on boundary lines, there is another group on the outer metropolitan fringe who are there because they desire the advantages of a central city for employment and recreation but prefer a somewhat rural environment in which to live.

Most cities and towns with populations of over 5,000 persons have some degree of "metropolitanitis," or the development of a substantial population residing on the fringe of a central

<sup>1</sup> U.S. Bureau of the Census, *1950 Census of Population*.

<sup>2</sup> Phillip H. Cormick, "Effects of Population Shifts," *Municipal Finance*, February, 1946, p. 25.

municipality. However, specific data are available only for cities of 50,000 population or more. The *1950 Census of Population* reports there are 168 metropolitan areas in the United States according to its definition of a metropolitan area.<sup>3</sup> These are all areas with large populations surrounding a central city with a population of at least 50,000 persons. A grand total of almost 84 million persons is involved.<sup>4</sup> Approximately 50 million persons reside in the central cities proper, and the remaining 34 million live in the fringe areas. A random sampling of many of the larger metropolitan areas together with their populations which reside either inside the central city or outside on the fringe is presented in Table 1. Also shown are the larger municipal income tax cities and the size of their central and fringe areas.

As a result of the shift to fringe areas, the historic source of municipal revenue, the real property tax, has been gradually weakened as an effective contributor to the current revenue needs. Many of the wealthy property owners have been involved in the so-called flight to the suburbs for the reasons previously cited, thus leaving behind fewer persons capable of paying property taxes. Blighted areas within

the average city have been increasing in size for many years, eliminating property once capable of providing a significant tax contribution. The historic lack of planning or zoning has also helped lessen property values.

Some cities began taking stock of this situation only after services began to be crippled for the lack of revenue.<sup>5</sup> Before that time there seemed to be recognition of the ever-increasing suburban population at the expense of the central city, but little has been done in the past to solve the dilemma. Chief reasons for inaction have been restriction of municipal authority to encompass territory within the city's economic sphere and/or political inertia on the

<sup>5</sup> For example, the income tax cities listed in Table 1 generally have stated that the nonresident problem was one reason for adopting their tax. The majority of the cities have not as yet acted on solving this problem. Among Table 1 non-income tax cities only New York, Los Angeles, San Francisco, Washington, and Sacramento have adopted significant new revenue-producing taxes to supplement property taxation. These particular cities are using the sales tax. The California municipalities selected sales taxes because it was felt that patterning the tax after the State of California sales tax would simplify the administrative complexity. The California municipal ordinances including the other 138 sales tax municipalities not listed in the table all provide that sales tax returns to the city are to be based on the amount of sales reported to the State within the city. Local auditing is eliminated because the State conducts its own auditing procedure in regard to its sales tax.

New York did show an interest in a municipal income tax in 1935 but dropped the proposed tax because of state legislative pressure.

The remaining units, except Washington D.C., are still relying almost exclusively on the property tax. Washington has an income tax similar to most state income taxes currently in effect. This information is based on an analysis of the Bureau of the Census *Compendium of City Finances in 1950*.

<sup>3</sup> U.S. Bureau of the Census, "U.S. Cities with Metropolitan Areas," *1950 Census of Population*. A standard metropolitan area contains at least one city of 50,000 population or more as of 1950, and each city of this size is included in one standard metropolitan area. One exception exists to this rule—in the case of the metropolitan area centering on New York City, the central cities are New York (7,835,099); Newark, N.J. (437,857); and Jersey City (300,477).

<sup>4</sup> *Ibid.* The total population of the United States in 1950 was 150,697,361. It had increased to 156,804,000 by June, 1952.



Table 1. Population of Representative Cities with Metropolitan Areas, and Percentage of Total Represented by Population Outside Central City, 1950

(In thousands)

Metropolitan areas	Total population	Population of central city	Population outside central city	Percent of population outside central city
<i>Non-income tax cities</i>				
New York <sup>a</sup> (N.E. New Jersey)	12,832	8,573	4,259	33
Chicago	5,476	3,606	1,869	34
Los Angeles <sup>a</sup>	4,339	1,958	2,382	55
Detroit	2,974	1,839	1,136	38
Boston	2,355	791	1,564	66
San Francisco <sup>a</sup>	2,214	1,141	1,073	48
Pittsburgh	2,206	674	1,532	69
Cleveland	1,454	906	548	38
Washington, D.C. <sup>a, b</sup>	1,458	798	660	45
Baltimore	1,321	940	381	29
Atlanta	664	327	337	51
Sacramento <sup>a</sup>	276	136	140	51
Trenton	229	128	102	45
Charleston, S.C.	160	68	92	58
Raleigh	136	65	71	52
Galveston	112	66	46	41
Waterloo	99	64	35	35
<i>Income tax cities</i>				
Philadelphia	3,661	2,065	1,595	44
St. Louis	1,673	852	821	49
Louisville	574	367	207	36
Columbus, Ohio	502	375	127	25
Dayton	453	243	210	46
Toledo	393	301	92	23
Johnstown	291	63	228	78
Scranton	256	125	131	51
Eric	218	130	88	40
Altoona	139	77	62	45
Springfield, Ohio	111	78	33	30
Lexington, Ky.	98	54	44	45

Source: Bureau of the Census, "U.S. Cities with Metropolitan Areas," 1950 Census of Population.

<sup>a</sup> Each of these cities is currently receiving significant revenues from the general sales tax to support the real property tax system. The remainder of the non-income tax cities are still relying substantially on the real property tax.<sup>b</sup> Washington also has an income tax to use in conjunction with the general sales and gross receipts taxes.

part of central city administrations to adopt a forthright plan to annex neighboring territory. The amount of fringe territory actually annexed by American cities in the twentieth century has been limited. This has been the case particularly with cities in the New England, Middle Atlantic, and Midwestern states. For example, Philadelphia has annexed only one-tenth of a square

mile since 1854. The present boundary of St. Louis has not changed since 1876. New York's boundary is the same today as it was at the time of World War I.

### Difficulties of Annexation

The annexation of unincorporated areas bordering central cities presents no problem. Complications arise when

the fringe area is incorporated into a separate municipality. Many cities have tried to annex neighboring districts, but the natural obstinacy on the part of nonresidents to approve annexation proceedings for fear of losing their identity or of having higher taxation has precluded any chance of major territorial acquisitions. Stipulations in most state laws require majority approval of the electorate or property owners located in populated contiguous areas. In New York the Constitution states: "No territory shall be annexed to any city until the people of the territory proposed to be annexed shall have consented to such annexation by a majority vote on a referendum called for that purpose."<sup>6</sup> In Illinois the procedure involves initially a petition signed by 250 of the electors of the municipality sought to be annexed.<sup>7</sup> If a majority of those voting in this contiguous municipality approve, then annexation awaits the approval of the annexing city. A failure to gain majority approval means that at least two years must pass before the same question may be voted on again. To effect an annexation in New Jersey a petition containing the names of at least 60 percent of the voters residing in the territory to be annexed must be presented to the governing body of the municipality to which such annexation is sought.<sup>8</sup> Then two-thirds of this governing body must approve before annexation may take place. In Indiana a

petition signed by 51 percent or more of the persons owning property in the territory seeking to be annexed must be presented before annexation may take place.<sup>9</sup> In Kentucky,<sup>10</sup> Michigan,<sup>11</sup> and Ohio<sup>12</sup> final approval of annexation rests with the majority of the electorate in the municipality or portion of a municipality to be annexed signifying their willingness.

Annexation has occurred more frequently in the larger cities of the South and the Southwest and in the smaller cities of California than elsewhere in the United States. In comparison with the rather insignificant amounts of territory that have been traditionally added to cities from neighboring territory, several of the acquisitions have been phenomenal. Atlanta is the outstanding example. This city, long besieged by an enormous fringe population in neighboring unincorporated areas, recently succeeded in adding 82 square miles of Fulton County, Georgia, containing a population of 100,000 persons.<sup>13</sup> Other cities annexing abnormally large fringe areas since 1945 have been Albuquerque, Dallas, Fort Worth, Houston, and Memphis. The smaller California cities have been able to accomplish annexations on a scale unparalleled in any other state as far as total number of cities involved is concerned. In many of the examples cited,

<sup>9</sup> *Burns Indiana Statutes Annotated*, Sec. 48-702.

<sup>10</sup> *Kentucky Revised Statutes*, Sec. 81.100.

<sup>11</sup> *Michigan Compiled Laws*, Sec. 117.6-117.14.

<sup>12</sup> *Ohio Code Annotated*, Baldwin's 1948 Revision, Sec. 3566-3570.

<sup>13</sup> John C. Bollens, "Metropolitan and Fringe Area Developments in 1951," *Municipal Yearbook*, 1952, p. 31.

<sup>6</sup> *Constitution of New York*, Art. 10, Sec. 14.

<sup>7</sup> *Smith-Hurd Revised Statutes*, Ch. 24, Sec. 7-13.

<sup>8</sup> *Revised Statutes of New Jersey*, Title 40, Art. 5.



the total population added has not been particularly large, but the additions have had the virtue of adding unincorporated neighboring territory before the population became dense in these areas. The ease of acquisition in the southern half of the United States as opposed to the difficulties already outlined for northern states has not been the result of favorable elections held among fringe area residents. It has occurred because of state legislative action.

However, annexation does not appear to be the answer for larger cities. Commuters in some cases travel as far as 50 miles from the place of residence to work. New York City would have to annex 365 square miles to include the area within a 15-mile radius, 2,827 square miles for a 30-mile radius, and 7,854 square miles for a 50-mile radius.<sup>14</sup> Philadelphia, Chicago, Boston, St. Louis, and the other large cities are similarly situated. For some cities the problem is further complicated because parts of the fringe areas lie in other states. Under the state laws as designed at present, there is virtually no possibility of a city in one state reaching across the state boundary to annex a contiguous out-of-state area. New York, Chicago, and Philadelphia, for example, face this problem of combining the political area with the economic area.

### Short-Run Solutions

The easiest short-run remedy probably lies in establishing a municipal tax system which recognizes that nonresi-

dents receiving sustained benefits from the central city owe some financial obligation to that city.

### Retail Sales Taxes

The retail sales tax has been mentioned as one method of exacting a contribution from those nonresidents who use the central city as a shopping center.<sup>15</sup> Such a tax does not seem to be a particularly practical method of taxing nonresidents because it may lead to the relocation of shopping centers beyond the central city's borders and to the shift of purchases from one area to another. Arguments to this effect arose in Philadelphia in 1938 when the city discarded its year-old sales tax. The merchants protested at that time that city businesses were losing out to suburban shopping centers which did not have sales taxation. There is reason to believe that in a number of cities retail business would lose many of the non-resident customers should a sales tax be put into operation, and the tax would fall short of its objective of re-

<sup>15</sup> Other than state or Federal grants-in-aid, probably only two types of taxes could bring in sufficient revenue. These two sources are the sales tax and the income tax. The retail sales tax is probably the only source of local revenues which could yield sufficient returns for the larger municipalities. Selective sales taxes on luxury or semiluxury commodities in general would produce minor revenues. Only a general sales tax without significant exemptions would produce sufficient revenues to qualify the source as a tax complementary to the real property tax. New York City and some cities in California, for example, have made extensive use of retail sales taxation. Many other cities have selective sales taxes on such items as tobacco, hotel rooms, restaurant meals, alcoholic beverages, and soft drinks. The taxes are not outstanding contributors to local revenues in most cities using these sources. See *Municipal Yearbook*, 1952, pp. 194-197.

<sup>14</sup> Mabel L. Walker, "Factors Affecting Municipal Revenues," *Municipal Finance*, August, 1947, pp. 15-19.

ceiving some payment from nonresidents for use of the city's facilities and services. New York City has experienced the problem of nonresidents transferring their shopping either to the suburban branches of New York City department stores or to other retail outlets in suburban New York or in the larger neighboring cities in New Jersey and Connecticut. California does not seem to have this problem since municipal sales taxation is found in most of the larger population centers of the state and shoppers are generally unable to take advantage of trading in a neighboring nontax city.

There are undoubtedly central cities the character of which makes it financially unsound for retail businesses to relocate outside municipal boundaries for the sole purpose of avoiding the imposition of a tax on retail transactions. In cities where retail trade has customarily been conducted on a large scale in downtown central shopping areas and where in turn the retail center is supplemented with entertainment and cultural features, it might be impossible for relocated merchants to induce an equal or an increased number of consumers to transfer their shopping to the suburbs. Serious inroads are nonetheless being made into the business of many downtown shopping centers because of the congestion problem and the widespread lack of parking facilities. The suburban retailers do have the advantage of parking facilities which, taken with the feature of tax-free purchases, may have a decided influence in decreasing the importance of the older retail centers in the central city.

### Income Taxation

An income tax levied both on residents and on nonresidents to the extent of their earnings allocable to the central city may be an answer in the numerous examples where a metropolitan economic area lacks any reasonable identification with the central city's political boundaries, especially if territorial acquisition cannot circumvent the problem. The case for also including residents under an income tax, other than the very important revenue consideration, stems from two points. First, to insure uniformity and to avoid discrimination in coverage it is necessary to include residents. Secondly, here is a long-awaited opportunity to place the municipal tax system on a sounder economic basis than it has been heretofore, at least during the twentieth century. It is common knowledge that in many cities real property ownership is no longer necessarily correlated with the community's wealth. Income is a base to be considered as important as the ownership of real property in municipal taxation. Thus the municipal income tax may also offer the opportunity to distribute more equitably the local tax burden in the light of the modern distribution of community wealth.

With an income tax it is doubtful that any significant transfer of employment will take place on the part of nonresidents who are currently employed in the central city. The income tax as it applies to the net profits of incorporated or unincorporated businesses has thus far remained at the very low rate of  $1\frac{1}{4}$  percent or less. It appears to be too small a factor to induce a major relocation of industry. How-



ever, higher rates than have been experienced so far might lead to the movement of small businesses or professional occupations that may not have large immovable capital assets. It is possible also that new industries or businesses of varied size and financial stature may not be willing to locate in a central city if the tax is high enough to affect profit margins seriously.

In the four states where municipal income taxation is found — Pennsylvania, Ohio, Kentucky, and Missouri — nonresidents are included in the income tax (or occupational license tax<sup>16</sup>) ordinances.<sup>17</sup> Justification for the inclusion of nonresidents has been that the tax is a payment for the opportunity the city has given them to earn their livelihood. Some of these cities have argued that they must provide essential services and facilities to encourage the establishment of industry within their borders. In order to do this the nonresidents employed within the city are asked to contribute a share of the expenses of paying for these municipal services which in turn make it

possible to have employment opportunities. Despite this seemingly convincing argument there is certainly merit to a counterargument that fringe-area residents are contributing an intangible benefit to the central city by making it possible for the city to have commercial and cultural advantages which it would not have without them. Unfortunately there is no measurable way of evaluating the contribution of these fringe residents to the increased economic and social values of central city property and to other valuations. A clearer distinction can be made for tax purposes between those nonresidents who occasionally use the city's facilities for consumer or cultural advantage and those who make daily use of the facilities in commuting to and from their places of employment and while at the place of employment. The former need not be taxed under the thesis that their contribution to the central city is offset by their occasional use of city services. The latter group does impose a sizable cost on the city, however. A large portion of municipal expenditures is used to maintain these services. These costs should be partially paid for by these nonresidents by the use of a very low rate income tax.

<sup>16</sup> In Kentucky the income taxes are called occupational license taxes in order to comply with the state constitutional requirements. However, the ordinances are similar to the income tax ordinances in effect in Pennsylvania and Ohio.

<sup>17</sup> Pennsylvania provides the best possible case study of municipal income taxation at present. Including Philadelphia, the most recent count lists a total of 263 separate municipalities and school districts including 10 cities, 66 boroughs, 185 school districts, and 2 townships. Eight cities in Ohio, four in Kentucky, and St. Louis, Missouri, are also currently taxing incomes. Pennsylvania's enabling Act 481 prohibits school districts from taxing nonresidents. The theory behind this prohibition is that school districts provide no direct services to nonresidents employed in the school district.

As an illustration of how the income tax program has been working in selected cities in regard to the fiscal contributions of nonresidents, it can be seen from Table 2 that significant revenues are being contributed by nonresidents. In comparison with the total municipal income tax revenues, the average contribution in a typical city is approximately 15 percent of the total. This is not an exorbitant penalty on



Table 2. Total Revenues of Income Tax Cities, Income Tax Collections, and Payments by Nonresidents, 1950  
(Thousands of dollars)

Tax Units	Total revenue	Total income tax collections	Collections from nonresidents	
			Amount	Percent
Philadelphia.....	\$126,026	\$37,500	\$5,625	15.0
Scranton <sup>a</sup> .....	3,520	764	17	2.2
Altoona.....	2,376	618	93	15.0
Johnstown.....	1,938	494	143	29.0
New Castle.....	1,060	371	63	17.0
New Kensington <sup>b</sup> (School District)	1,222	132	.....	.....
Toledo.....	17,098	6,787	450	6.6
Columbus.....	12,992	3,053	434	14.2
Dayton.....	10,571	1,766	353	20.0
Louisville.....	28,104	5,538	831	15.0

Source: Data for this table were collected from the municipal income tax collectors, the chambers of commerce in the cities listed, and the Pennsylvania State Employment Service.

<sup>a</sup> The City of Scranton is surrounded by 37 subdivisions which also have income taxes. Since Pennsylvania Legislative Act 481 gives priority to a person's place of residence rather than to the place of the income's origin if both units have the tax, Scranton receives only a very small contribution from its nonresident employees.

<sup>b</sup> New Kensington School District and other Pennsylvania Act 481 income tax school districts are not permitted by law to tax nonresidents.

nonresidents by any means, and it gives little cause for complaint on their part that central cities are attempting to shift the burden of their tax program onto foreign shoulders.

Little opposition has come from nonresidents in the form of a direct protest. In Philadelphia during the early history of the tax some nonresident workers claimed that the income tax ordinance was "taxation without representation." Philadelphia answered that both the nonresident's place of domicile and the location of his employment have come about because of his voluntary choice and that the status of either may be changed if he so desires. This seems to be a fair answer.

1. *The Population Density of the Fringe.* There may be a question of how densely populated a fringe area should be before it becomes necessary

for the central city to include nonresidents in an income tax ordinance. Much depends on the proportion of total municipal employment represented by nonresidents. Where the number is substantial it is indicative that much of the income created locally is being carried away from the city. Where the line should be drawn would be difficult to tell. However, much would depend on the relative strength of the economic base as represented by income and by property located within the central area. Substantial sources of property wealth which can be equitably taxed, in addition to a large internal working population representing a large annual income base, perhaps may be considered in deciding whether it is imperative to tax nonresidents.

2. *Central City Size as an Administrative Consideration.* The question

which logically follows from the selection of an income tax is, Is a city or other municipality too small a governmental unit to administer an income tax successfully; and if there is reason to suppose that certain municipalities are administratively capable, is there any particular size of population which would be more suitable for the adoption of the tax? Pennsylvania is one state where there have been few barriers to the size of a municipality permitted to tax earned income. Philadelphia, with a population of 2,071,605 persons, is the largest unit. At the other extreme are 107 units in Pennsylvania with populations of less than 2,500 persons. In between the two extremes are municipalities of varying size.

Concerning the thesis that the ability of a municipality to administer the income tax depends partially on its population size, experience to date does not support the conviction that the larger the political subdivision, the more effectively the administration can be handled. If it is true that larger municipalities will have less administrative difficulty than the smaller units, Philadelphia should have been somewhat more successful than the much smaller municipalities. In view of the problem cited long ago by Professor Seligman—that even the state is too small a governmental unit in which to apply effective collection machinery<sup>18</sup>—it appears that municipalities would have considerable difficulty in collecting the tax. This difficulty would be progressively greater from the larger to the smaller municipalities.

However, as the current pattern of taxation stands, only earned income is taxable and income from investments and other unearned sources is exempt.<sup>19</sup> This restriction of taxation to “wages, salaries, other compensation, and net profits” eliminates ferreting out unearned income from frequently obscure sources outside the municipality.

All the ordinances in use compel employer withholding for businesses located within the taxing city. The income which is withheld by employers for their employees accounts for approximately 75 percent of all local income tax revenues. Where most of the income is withheld and there is no taxation of unearned income, the size of the municipality does not appear to be very important. Philadelphia has had no greater or lesser success in obtaining compliance from resident employers than the smaller municipalities where employers’ withholdings are dominant.

It is with the remaining 25 percent

<sup>19</sup> One solution for overcoming the problem of the administrative incapability of cities’ taxing unearned income as well as earned income is the adoption of an income tax supplement system. Under this arrangement either the state or the Federal government, depending on the agreement, would administer the tax for the municipalities by collecting the revenues for the latter government. The tax rate is established locally by whatever means is provided and is merely added to the state or Federal tax rates within the limits set by state or Federal law. A further advantage is that municipalities of varied size could use supplements. The smaller cities where administrative ability seems to be lacking in most cases to control adequately a local income tax which in the future might possibly include exemptions, graduated rates, and unearned income are saved the cost of setting up expensive collection machinery which otherwise would be necessary.

<sup>18</sup> E. R. A. Seligman, *The Income Tax*. (New York: Macmillan Company, 1911), p. 425.

that some difficulty is found in obtaining compliance. This latter group is composed of those persons who are required to file returns individually. Size could make a difference in the handling of these separately filed individual income and net profit accounts. Philadelphia has not efficiently administered this latter area, according to the findings of several investigative agencies including a Philadelphia grand jury in 1948. Residents working outside Philadelphia have been the principal source of evasion, and they are followed closely by self-employed residents, Federal and state employees, nonresidents not subject to withholding, professional men, and owners of unincorporated businesses. This is the same problem found elsewhere in Pennsylvania, Ohio, and Kentucky. However, despite the apparent collection difficulty experienced with this 25 percent of the total tax that is not withheld, it is estimated that only about 20 percent of the tax due is not being paid—that is, 5 percent of the total income tax due.

The corporate net income tax, which is found thus far only in Ohio, Kentucky, and Missouri (St. Louis), has not been tested in the very small municipalities since Pennsylvania, with its small income tax units, does not permit its local governments to tax corporate income. It appears that the population would make little difference if a corporation were located within the boundaries of the municipality. It is with the corporations located elsewhere which are doing only a portion of their business in the taxing municipality that size might be a determining factor in

obtaining compliance. This is so because it is possible for the larger municipalities to establish much more elaborate collection machinery. Larger investigative or auditing forces can help reduce the degree of evasion.

An extensive investigation of numerous smaller municipal income tax administrations indicates one advantage in tax collection these smaller units in Pennsylvania seem to enjoy over large cities such as Philadelphia, Louisville, Columbus, and Toledo.<sup>20</sup> This is the ability of tax administrators or other municipal employees to know many of the circumstances concerned with the income and employment of certain residents and nonresidents earning income in a particular unit.<sup>21</sup> This is an informal investigative technique that has gained many additions to the income tax rolls which might have escaped detection in a large city. Even in the fairly large city of Dayton, tax officials believe that this technique is important in keeping evasion at a minimum.

The efficiency of administration can overcome much of the otherwise varied differentiation in populations based on the historical experience with the municipal income tax to date. Should the income tax be made more complex by the addition of unearned income, progressive rates, deductions, and personal

<sup>20</sup> This conclusion is based on the results of a field trip to more than thirty local income tax units and also on correspondence with income tax officials in numerous other local units.

<sup>21</sup> Examples of this method include knowledge of personal business transactions of neighbors, of newspaper reports and classified advertising, and of new residents moving into the neighborhoods of municipal employees.



exemptions, there is every reason to believe that the smaller cities could not adequately handle the added burden.<sup>22</sup> Income tax officials in Columbus, Dayton, and Springfield, Ohio, doubted that they could administer this type of income tax. The common belief is that the cost of effective administration would exceed collections. As the tax now stands in all municipalities with its low rates and lack of progression in rates and exemptions (except in Springfield, Ohio<sup>23</sup>) and with its application to earned income only, the differential in administration between large and small municipalities has not been significant.

3. *Limitations of a City's Economic Base.* Certain other exceptions need to be considered before concluding that the income tax is or is not the answer to every central city's fiscal distress. In some cities, property ownership is necessarily the chief indication of community wealth. In other cities, different measures would be more appropriate. For example, in Altoona many of the

property owners are retired railroad pensioners existing on very modest annual incomes. Exclusive reliance on real property taxation would be grossly unfair since this very active railroad city maintains a tremendous number of transient employees who own no local property but earn their income as a result of the economic existence of Altoona. Here a tax on earned income has justification. Yet in communities which exist almost wholly for retirement purposes and where earned income represents only a small portion of community wealth such a tax could serve little purpose. Certain Florida or southern California communities are good examples of cities catering to the retired. Here property taxation supplemented by perhaps an amusement tax may be more suitable than any form of income taxation.

In other cases, the fact that cyclical fluctuations or temporary work stoppages in the national economy or in local or regional economies are more likely to have disastrous effects on cities supported by one or two industries requires considerable thought as to the desirability of a city's placing too much emphasis on a revenue source that diminishes proportionately with increasing unemployment. This revenue shortage can only mean a curtailment of essential municipal services. No better example can be offered than the experience in the past four years of certain Pennsylvania and Ohio cities which have relied heavily on municipal income tax revenues. Keeping in mind that more than half of the Pennsylvania income tax units are in coal-mining and steel-producing areas and that several Ohio cities are also in steel-

<sup>22</sup> Long ago Adam Smith in commenting on the administration of a tax objected to taxes that "may require a great number of officers, whose salaries may eat up the greater part of the produce of the tax, and whose perquisites may impose another additional tax upon the people." See *The Wealth of Nations*, Vol. II, Book V, Chapter II, Part II (Modern Library ed.; New York: Random House, 1937), p. 778. This same objection may be leveled against the extensive municipal income tax administration which would be necessary to administer a more complex form of income tax than currently exists.

<sup>23</sup> Springfield has justified its \$1,040 individual exemption for administrative convenience only. It eliminates the hundreds of small accounts of part-time workers which have caused administrative difficulties in obtaining compliance.

producing areas, it is necessary to observe what happened during the prolonged strike periods in late 1949 and more recently in June and July, 1952. Income tax revenues decreased by thousands of dollars during the course of the strikes in such cities as Johnstown, Altoona, Erie, and Youngstown. These cities are not diversified enough economically to maintain a balanced income tax revenue. Philadelphia, Louisville, St. Louis, and Toledo, for example, are in a much less precarious position. Their industrial diversification should almost guarantee fairly stable income tax receipts in the event of a strike in one or two of their major industries.

4. *The Ability-to-Pay Principle.* As the tax ordinances currently stand, the individual-capacity-to-pay principle has been ignored. Because exemption and progression features are absent (except in Springfield, Ohio) and because the tax is applicable only to earned income, the person with a family of ten pays as much tax as a person with the same gross income who has no dependents. The general effect of proportional rates is to ignore the principle of equality of sacrifice.<sup>24</sup> The omission of unearned income, which accrues in the main to persons with larger incomes, extends the present inequality of treatment still more. It may be argued that the Federal government is taking care of the

problem of equality of sacrifice with its steeply progressive income tax so that municipal governments need not bother. However, despite the relatively light local rates there is some justification in attempting to align the local income tax with the Federal, state, and local tax structures in the general framework of over-all tax equality.

However, one point in favor of the present system of income taxation is that it reduces administrative complications which would otherwise be difficult to contend with. For example, differences in family responsibilities, which are of major importance in striving toward equity through equality of sacrifice, should probably be considered, but such allowances would add substantially to the administrative difficulties.

It can also be argued that the flat-rate, exemptionless tax currently in use is more in line with ability to pay, or less regressive, than property taxation. There is often no relation between a property owner's ability to pay and the property tax assessed against him.

### The Role of Property Taxation

Assuming that the income tax gains wider acceptance in the near future, the question arises as to what is to be the role of the property tax in the central city financial structure. It is generally accepted that property taxation leaves much to be desired in regard to efficiency of administration. Inefficient tax personnel, chronic underassessments, and inequality of treatment between owners of different types of property are general accusations leveled at the local property tax system. The question then arises, Will the

<sup>24</sup> The principle of equality of sacrifice is included in the doctrine of ability to pay. Briefly stated, the principle establishes a general, over-all rule that the loss of economic goods (through taxation) becomes less important as people acquire more of them. Implicit here is the idea that protection should be offered to families in order that they may satisfy their most urgent wants without tax penalty.

addition of the income tax in a central unit tend to postpone efforts to improve or at least maintain the current efficiency of property taxation? This is a serious problem because the current history of municipal income taxation indicates clearly that a rate as low as 1 percent of gross individual earnings and of business net profits is capable of yielding as much as 30 percent of total municipal tax revenues. These yields are substantial and may be large enough to sidetrack any concerted interest in improving the property tax structure or at least maintaining the status quo. The results of an exhaustive survey of the existing income tax cities reveals that little has been done to improve assessments and collections of the real property tax. In many of these cities property tax revenues have increased since 1948, but few of these increases are traceable to an over-all community reassessment program. The additions of new properties to the assessors' lists and some increase in real property tax rates have been responsible for the revenue increase.

Reassessments are costly operations. This is one of the reasons why assessed valuations have not kept pace with market valuations in recent years. For example, the total local assessed valuation in Pennsylvania in 1949 was only 29 percent of the total market value of all taxable real property.<sup>25</sup> Revisions

lagged as much as ten years behind the fluctuations in the selling prices of real property. This lag is found throughout most local governments and is one of the principal reasons advanced for improving the administration of the property tax.

Some doubt is expressed that improvements will come as quickly in income tax municipalities because the new revenues tend to postpone the reorganization of the property tax system so long as sufficient revenues are being made available from this new source. This is a danger which should be recognized and guarded against lest the assault on nonresident and resident income to effect a more equitable municipal tax structure bring about the further collapse of the tax which historically has been the foundation of local taxation.

### A Long-Run Solution

In addition to weighing the merits of municipal income taxation in central cities, attempts should be made technically to dissolve the political boundaries. Recognizing that many municipal boundaries do not encompass the entire economic area of their vicinity, it is suggested that the tax administrative area be enlarged to include the whole metropolitan area if the central municipal political area cannot be enlarged through annexation. In the case of metropolitan economic areas, joint administrative arrangements between the central city and fringe political subdivisions could be used profitably by both the urban and the fringe units. These administrative agreements may include tax-shar-

<sup>25</sup> The reassessment made by the Pennsylvania State Tax Equalization Board in 1949 was solely for the purpose of determining the amount of state educational aid to be paid to the individual school districts. The assessment figures were not accepted by the school districts or the county governments for their use except in isolated cases.



ing arrangements as well as utility, health, educational, and other municipal services which might easily be shared. Current plans to streamline local governments in order to make the subdivisions politically and economically more functional than they have been in the past are still progressing slowly throughout the United States.

Atlanta and neighboring Fulton County, Georgia, are involved in the most progressive local government consolidation and cooperative program yet developed in the United States. This city-county administrative arrangement is known as "The Atlanta Plan for Improvement." With early arrangements completed in late 1951 and early 1952 the plan is now in full operation. The first step has already been mentioned. This involved the annexation of 82 square miles of fringe territory to Atlanta. In addition, a realignment of city-county governmental operational functions has been effected. Atlanta takes over, both for the city and for the county, police and fire protection, recreational facilities, and water, sewage, and garbage services. Atlanta also gains control of the county school system. The county gains complete control of the welfare programs and public health services. To oversee the "Plan," a joint performance committee has been formed composed of city, county, and school representatives.

The Atlanta program is the best example of a movement toward long-range functional municipal-metropolitan government. There are other cooperative regional administrative plans which are distinct signs of a trend toward functional local government.

The Bi-State Development Agency established in 1949 between Missouri and Illinois has as its purpose the future planning and development of the metropolitan St. Louis area in regard principally to various transportation facilities as well as water, sewage, recreational, and land-use programs. This interstate compact includes an area of 3,000 square miles, 225 municipalities, 750 local taxing districts, and a total population of 1,750,000 persons.<sup>26</sup> The agency has no taxing power.

Other compacts of similar nature are the veteran Port of New York Authority and the Delaware River Authority recently approved by Congress. Both of these interstate organizations are concerned with the development and improvement of port and other transportation projects in the metropolitan New York and Philadelphia areas, respectively. Thus, aside from the very promising Atlanta Plan, metropolitan functional arrangements are limited to only a few specific services. They are forerunners to the anticipated trend of metropolitan all-inclusive political and economic functional governments of the future.

It might be possible to adopt an income tax in the central city on all who are receiving income from sources within the city, including nonresidents, and then to establish some sharing ratio mutually satisfactory to cooperative fringe governments by which revenues could be distributed among all gov-

<sup>26</sup> The area includes the City of St. Louis, the counties of St. Louis, St. Charles, and Jefferson in Missouri, and the counties of Madison, Monroe, and St. Clair (East St. Louis) in Illinois.

ernments concerned. Toledo's plan, although it has not had a chance to be placed into operation, would retain 50 percent of the nonresidents' tax payable to the city and would return the other 50 percent to the taxpayer's domicile, provided like treatment would be given Toledo residents. With this type of plan, recognition would be given to a nonresident's tax responsibility to the locality of his employment and at the same time a portion of his taxes would be returned to the subdivision which also is providing municipal services for him. A plan of this nature would appear to be more satisfactory to fringe area residents and counteract the bitterness of the "taxation without representation" charge. Also it would reduce considerably the possibility of widespread double taxation of income if municipal income taxation should be adopted on a mass scale in the near future by central cities and other municipalities bordering on central cities. Without a common pattern of agreement extreme hardship will be experienced by persons living in one income tax city and earning income in another unless reciprocal arrangements can be made granting credit in one income tax unit for all or part of the tax paid to another.

Metropolitan intermunicipal arrangements both in tax and other potential joint municipal enterprises or endeavors are a more general solution than the immediate adoption of a tax such as the central city income tax. There is greater flexibility in the types of arrangements possible, plus a temper of mutual respect on the part of the metropolitan political subdivisions concerned.

Both the short-run and the long-run remedies suggested appear to be reasonably logical answers to the fostering of a more enlightened approach toward a progressive tax policy in metropolitan economic and political areas which fail to coincide. However, logic is oftentimes something of an elusive commodity in the field of modernizing municipal finance. The failure of many central core cities to battle their way out of their financial problems probably rests with the legislative or constitutional controls found in most states. Hence many of the suggestions made in this article would necessarily await state sanction. It is hoped, however, that a new interest will arise in the near future to allow these central municipalities a reasonable opportunity to build an equitable tax system to meet the changing times.

# How Many Managers Are There?

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DURING recent years, more and more attention has been focused on the problems of management in American business and industry. The literature in this area has increased tenfold and programs of management selection and development have been introduced in nearly every major industry. Despite the attention which has been focused on this field, almost no effort has been made toward quantifying the managerial components.

How many executives are there in the average American business institution? What percentage of the total work force is engaged in managerial occupations? What percentage of this managerial group holds minor managerial positions? What percentage holds executive positions? Are there managerial structures which are characteristic of sizes or types of businesses? Do wholesalers put more stress on managerial positions than retailers or manufacturers or service organizations? How many managers are there and how many managers should there be? These are some of the questions which have been raised over the years and which remain unanswered to date.

Very large economies of time, money, and manpower have been ef-

fected at the operator level in American business as a direct result of detailed analysis and study of work, jobs, and job relationships. Through research of this type at the operator level, the productivity of the average worker has doubled in less than two decades, with better working relations throughout. There has been no comparable research aimed at the problems and relationships of the management group, and this is the group where any minor improvement would be multiplied several times over. It must be remembered that the effectiveness of one member of the management group is reflected by a dozen, or even a thousand, workers at the operator level.

With questions such as these in mind, the present study was undertaken. The study was not designed to give final answers to all or any of the questions framed, but it was hoped a pilot study would indicate profitable lines for further research and perhaps develop some techniques through which valid answers might be obtained in larger samples.

The study was undertaken under the auspices of the Business Management Service of the University of Illinois in 1951. The format was developed by the authors and the methods were



checked with the management staff at the University. All interviewing was conducted by one of the authors — a graduate student working for his doctorate. In a survey of this type, the interviewer and the rapport he is able to establish with those interviewed are at least as important as the questions and the format of the study itself. It is obvious that complete confidence must be established from the start if valid responses are to be obtained, since answers to many questions consist of information which is confidential in nature.

Because the study was to be a pilot investigation, firms were selected on a carefully controlled cross-sectional basis. One hundred Midwestern firms were included in the original sample. These firms were located in Chicago, Detroit, Cleveland, and St. Louis. The sample was selected on the basis of size (defined by number of employees and gross dollar volume) and included very large, large, medium, and small businesses in numbers roughly proportionate to their national representation. The selection of firms on the other axis, by type of business, was handled in the same way; four classifications were set up on a proportionate basis: retailers, including only department stores and major retailers; processors, including large and small processors and wholesalers of food and allied products; manufacturers, with the emphasis on metal manufacturers; and service and financial establishments, including banks, insurance companies, and transportation organizations. When the final evaluations and tabulations were made, it was found that 82 of the 100 firms

included in the test sample had submitted complete and verified information. This report is based on those firms only.

One of the most difficult tasks in the entire project was the development of a suitable form for use in the interview. The questions included had to be exhaustive enough to get the required facts and yet not so detailed that the interviewer would lose rapport with the persons with whom he talked. In the final form, 20 questions were included and the average interview required two to three hours. In the smaller firms, it was necessary to talk with only one top executive — usually the owner of the firm — to secure the required information, but in the larger companies, the interviewer talked with as many as six or seven top executives. In every case, the interview was set up in advance by a letter describing the project and emphasizing the point that this was a confidential survey being conducted through the University of Illinois.

Questions covered general areas such as products handled by the company, gross profit figures for two years, whether the firm was a branch or a parent organization, seasonal employment fluctuations, and total number of employees. From this point, the interview moved into specific questions regarding managerial personnel. Questions included covered the number of major departments represented in the company, and the numbers of titled officers, major executives, minor executives reporting to the first-level managerial group, managers and supervisors, foremen and operating-level

supervisory personnel, and specialists and technicians not actually carrying a supervisory title but exercising certain managerial prerogatives. Each managerial level was defined in detail during the interview, and every effort was made to reduce each level of management to a common denominator so that comparisons between different types of businesses would be valid, irrespective of the titles which individual management personnel might carry. While this was the most difficult phase of the entire study, the problem of definition was solved effectively.

The 82 firms included in the analysis employed a total of more than 500,000 people. Although the sample is small in terms of number of firms included, it is felt that the base of more than half a million employees is large enough to provide a reliable index of general trends and differences. The smallest-sized firms employed as few as 10 workers, whereas the largest employed more than 150,000. Since the majority of American businesses fall in the "less than 500" category, almost half of those included in the survey were selected from this size classification: 36 firms had less than 500 employees; 11 had between 500 and 1,000 employees; 15 had between 1,000 and 5,000 employees; and 20 had 5,000 employees or more.

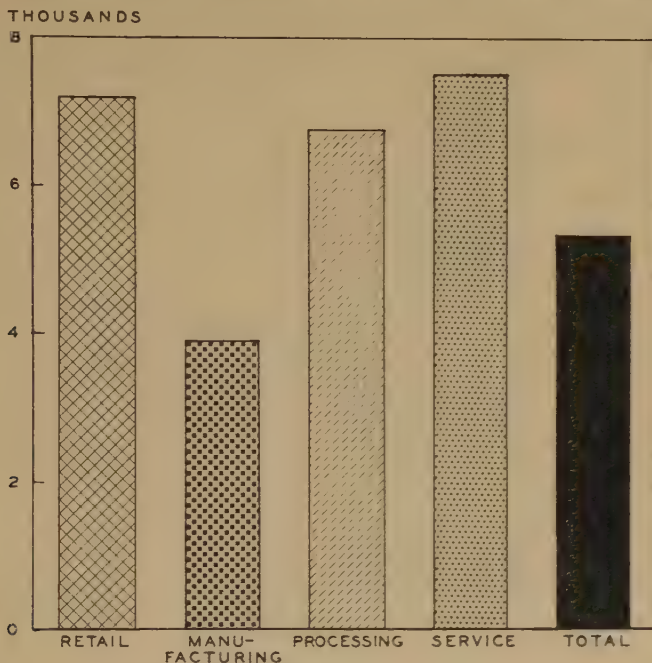
The breakdown of the total into types of businesses was as follows: 13 in the service and financial classification, 6 in the retail and department store classification, 17 in the processing classification, and 46 in the manufacturing and production classification.

### Findings by Type of Business

Over-all results from the survey show that 13.3 percent of the more than 500,000 employees had managerial responsibilities. For the total group, only 0.1 percent were "titled officers," that is, employees carrying such titles as president, vice-president, and secretary in addition to their operating titles. Another 0.2 percent were classified as "major or top executives." The largest number, 9.5 percent, were "managers, department heads, or supervisors." The final group, "first-line supervisors or production foremen," made up 3.5 percent of the total. While these four breakdowns were useful in obtaining accurate figures from the companies surveyed, it was felt that it would be more meaningful in this pilot report to combine the managerial classifications into two broad groups: "executives," including titled officers and major executives, and "supervisors," including managers, supervisors, operating heads, and foremen. These two categories conform roughly to the grouping used in the literature on the subject and are usually called "major executives" and "supervisors." The report of this preliminary analysis is concerned with these two major classifications primarily and figures refer to these combined groups. There was a third group to be considered, that of the "technician" who has some managerial responsibility. References to this third group are specifically labeled.

In considering management proportions by type of business, it is first necessary to establish the comparability of the groups in question. In Chart 1

Chart 1. Average Number of Employees, by Type of Business



the four types are presented in graph form showing the *average number of employees* in each type. As can be seen in this chart, the average retail firm employs 7,200 people.<sup>1</sup> In the manufacturing group, the average number of employees was 3,900; in the processing group, 6,800; and in the service group, 7,500. The average for all 81 firms was 5,300 employees. The manufacturing group had the smallest average number of employees because the inclusion of more firms in the manufacturing sample had the effect of increasing the number of firms in the

smaller-size category. With the exception of the manufacturing group, the average numbers of employees for the different types were remarkably similar.

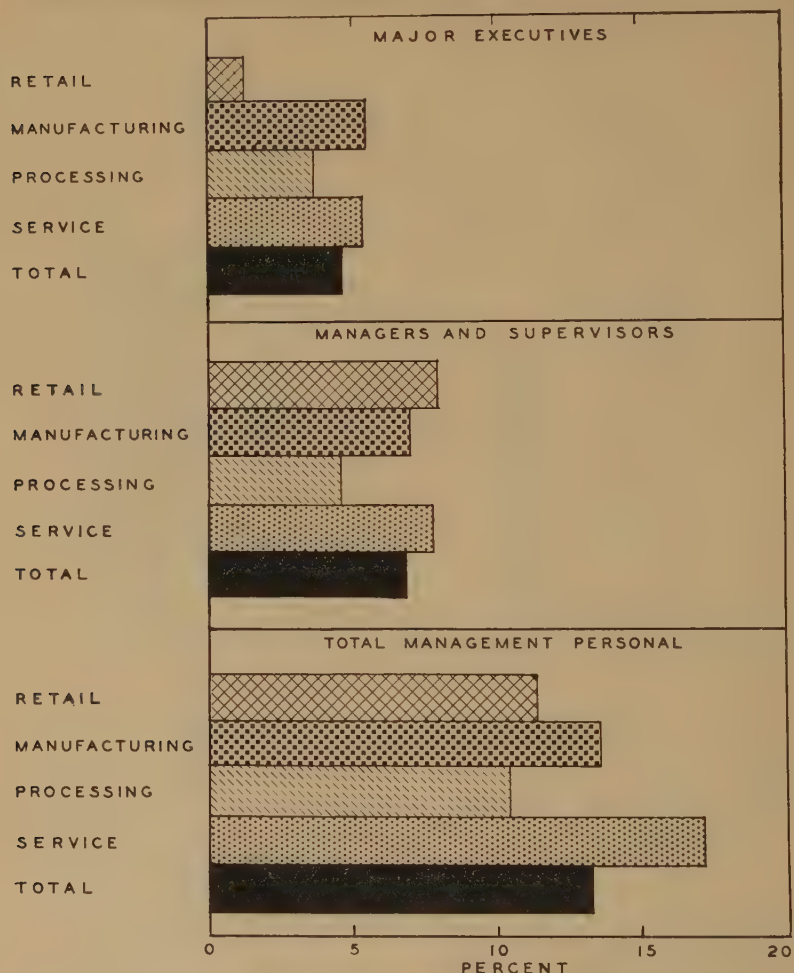
In the first panel of Chart 2, the proportions of *major executives* are shown by type of business. These are presented in percentage form; the actual figures are as follows: retail, 1.3 percent; manufacturing, 5.4 percent; processing, 3.9 percent; and service, 5.3 percent. The average for all groups was 4.8 percent.

The pattern for executives differs most from the average in the retailing area and this can probably be explained on the basis of known organizational practices in this field. The common pattern in retailing, particu-

<sup>1</sup> One firm was excluded from the retail employee sample because it had more than 10 times as many employees as the other firms included.



Chart 2. Proportion of Management Personnel, by Type of Business



larly in the department store, is to have the largest share of the managerial job performed at the operating level under the direction of a few top executives. The other group which differs markedly from the average is the processing group. The proportion of major executives in this group is also well below the average and indicates less emphasis on the top-level positions than is found in either manufacturing or service organizations. The differences between retail-

ing and processing and the other groups are significant.

The findings with regard to *super-*  
*visors* are presented in the second panel of Chart 2. The percentages of supervisory personnel by type of business are as follows: retailing, 8.0 percent; manufacturing, 7.1 percent; processing 4.8 percent; and service, 7.9 percent. The average for all groups was 6.8 percent.

It can be seen in Chart 2 that re

tailing makes up for its light top management coverage by a significant increase in the percentage of supervisory personnel. The processors, on the other hand, are below the average once more and even further below in this case than they were for top management personnel. Manufacturing is slightly above the average and service is significantly above the average. The findings for *all managerial personnel* including top management, management at the operating level, and technicians with managerial responsibility are presented in the third panel of Chart 2. The percentage figures are as follows: retailing, 11.4 percent; manufacturing, 13.6 percent; processing, 10.5 percent; and service, 17.1 percent. The average for all groups was 13.3 percent.

The over-all pattern shown in Chart 2 indicates that the percentage of managerial personnel for processing and retailing is well below the average. At the other extreme, the service group is much more heavily staffed than the other three groups, having one-fourth again as many in managerial positions as the average. The manufacturing group is nearest to the average point—partially because of its size—and appears to be setting a pattern.

There seem to be significant differences in managerial patterns by types of business. These differences are recognizable at the top level and through the lower levels of the managerial hierarchy as well. The retailers have the most variable pattern in that it underweights top-level positions and overweights operating-level positions.

Although these figures are based on relatively small samples, it is believed that the differences are large enough

to indicate valid trends. It should be stressed, however, that variations within each type of business are quite large and the average indicates only a general trend.

### Findings by Size of Business

There has been a good deal of material in management literature concerning the “average” percentage of managerial personnel employed by American businesses. There have been wide discrepancies between figures quoted in these studies, the range extending from a low of 5 percent to a high of 20 percent. It would be expected, on a purely pragmatic basis, that there would be wide differences in the proportion of managerial personnel in individual businesses and that these differences might be directly related to the size factor. It was with this thought in mind that the analysis of the managerial figures by size of business was undertaken.

Most of the “principles” upon which we have erected our managerial structure have no firm basis other than their ability to meet the practical test—i.e., American business, in general, continues to prosper, therefore the managerial principles and formulae must be correct. There have been a few attempts to develop a theoretical rationale for the managerial hierarchy. The most widely quoted of these attempts was that of Henry Fayol who built up a strong case for his thesis that the optimal ratio of workers to managers was seven workers to each manager, regardless of the size or type of business. In percentage form, this would mean that about 14 percent of those employed in business today should be in

the managerial ranks. It is interesting to note that despite the fact that most of Fayol's critics have said that his figure was much too high the findings of this pilot study indicate that it is supported by fact. Where Fayol suggested 14 percent as the correct proportion of management, the actual figure for this sample is 13.3 percent.

The percentage of managerial personnel is inversely related to the size of the organization. This is, of course, the result of deliberate planning. One of the basic tenets of "big business" has always been that profits can be increased by increasing the size of the business and spreading the managerial personnel thinner as the business grows. It would be interesting to test this "accepted theory" on a larger sample and compare rate of profit for businesses of comparable size having different degrees of managerial saturation.

In reporting the findings of this survey, several size groups were experimented with in an effort to find comparable grouping. Although there were wide differences among some of the smaller businesses, there were four breakdowns which were most cohesive. Within these four classifications, the individual businesses seemed to have more in common than in the finer subdivisions. The size categories finally used in this report were the following: less than 500 employees; between 500 and 1,000 employees; between 1,000 and 5,000 employees; and 5,000 employees or more. Since the sample was relatively small, no attempt was made to break down the samples by type of business within these size categories.

The proportions of *major executives*

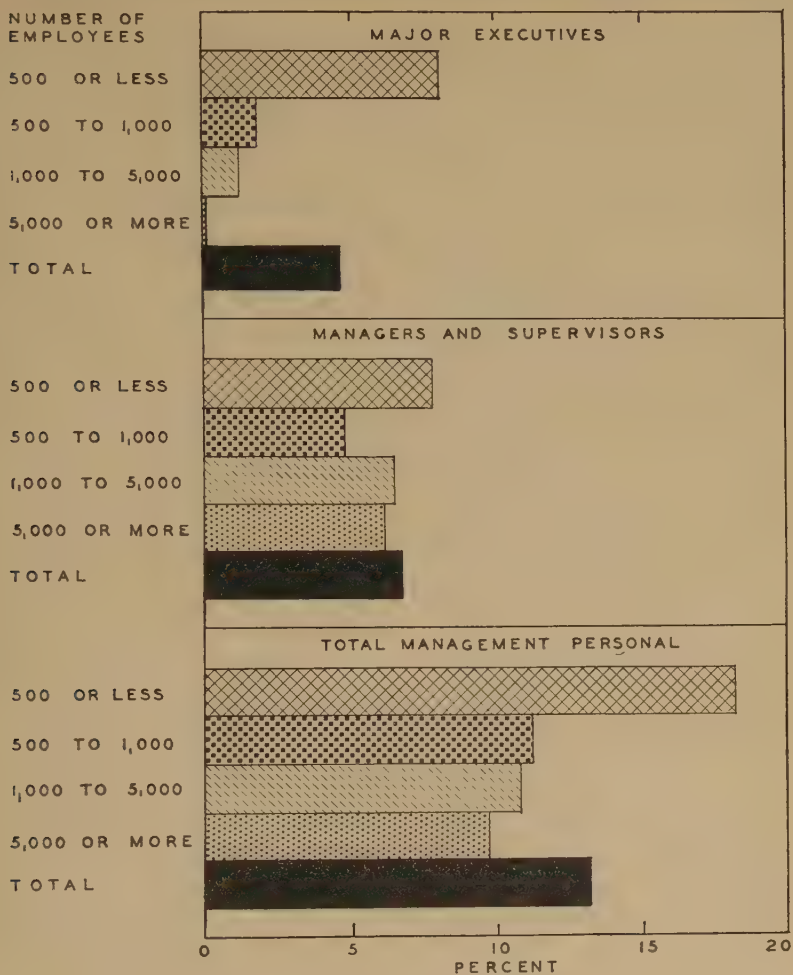
by size of business are shown in the first panel of Chart 3. The four size categories had the following percentages of top management personnel: 500 workers or less, 8.1 percent; 500-1,000 workers, 1.8 percent; 1,000-5,000 workers, 1.3 percent; and 5,000 workers or more, 0.2 percent.

As might be expected, the smaller businesses have a larger percentage of top management personnel than the larger businesses — primarily because the smaller organizations are managed and operated to a greater extent by owners and their immediate families. Most interesting of all is the inverse relationship of the percentage of top management personnel to the size of the business. Although the sample is small, the regularity of this trend can hardly be explained by chance. While the general outline of this relationship has been recognized for many years, this is first-hand documentation of the accepted fact indicating the contour of the relationship, which decreases from a high of 8.1 percent in the smallest establishments to a low of 0.2 percent in the larger businesses. The average for all groups was 4.8 percent. This average is perhaps artificially inflated by the smaller businesses with their large proportions of top management. The average for the larger establishments is less than 1 percent.

When the percentage of *supervisory personnel* is examined, no regular pattern is found as in the case of figures for top management personnel. The findings for the supervisory group are presented in the second panel of Chart 3. The percentage figures are as follows: 500 workers or less, 7.9 percent;



Chart 3. Proportion of Management Personnel, by Size of Business



500-1,000 workers, 4.8 percent; 1,000-5,000 workers, 6.7 percent; and 5,000 workers or more, 6.3 percent. The average percentage of supervisors and foremen for the total group is 6.8 percent.

It is rather surprising to note that the smaller establishments have the highest proportion of managerial personnel on the second level. There is a significant drop below the high of 7.9 percent for the "500 or less" group to 4.8 percent for the "500-1,000" group.

This drop is the only break in the pattern, but it is more apparent than real since nearly 5 percent of the employees in firms of this size were classified as "technicians, specialists, and other non-supervisory personnel." In other words, these firms are going through a transition period and delegate considerable supervisory-level activity to specialists who do not carry operating managerial titles.

The proportions of *all managerial*

*personnel*, including top management, supervisors, and technicians having managerial responsibility, show the same pattern of regularity as those displayed in the first panel of Chart 3. The third panel of Chart 3 shows the comparative differences for all managerial positions by size of establishment. These figures are as follows: 500 employees or less, 18.4 percent; 500-1,000 employees, 11.2 percent; 1,000-5,000 employees, 10.8 percent; and 5,000 employees or more, 9.9 percent.

As was noted earlier, an inverse relationship exists between the percentage of total managerial personnel and number of total employees. The average percentage of managerial personnel for all groups was 13.3 percent. This average figure is probably artificially high because of the disproportionate emphasis on the "500 or less" group. The chart shows graphically that the smaller establishments are putting more stress on, and undoubtedly paying more for, their managerial personnel than are the larger businesses. If the smaller group were excluded, the average for the larger institutions would be approximately 10.5 percent. The findings indicate certain definite and recurrent trends which in all probability are directly related to the size and complexities of modern business.

### Summary

While the sample used in this pilot study was too small to permit detailed breakdowns, it was large enough to indicate certain characteristic differences.

When examined in terms of type of business, there can be little doubt that

the characteristic pattern for retailing is quite different from that of manufacturing with regard to the proportion of managerial personnel — whether considered in total or by breakdowns of the total. There is little doubt that the occupational structure of the processing business is significantly different from that of other types of businesses. There is a noticeable trend for service and financial firms to increase the emphasis on managerial positions at each level. Business size and its relationship to the percentage of managerial personnel is one of the controlling factors in the organizational structure of modern businesses. The pattern of differences is too regular and consistent to be the product of chance.

This is particularly true with regard to top management personnel and to total personnel engaged in managerial positions at all levels. This has real and practical application in many fields. One of the obvious practical implications is for the college counselor who is endeavoring to advise graduating college people in search of managerial positions. Percentagewise, the chances are almost twice as good for managerial positions in smaller businesses as compared with larger businesses. Although there are more managerial jobs in large businesses numerically, the competition is keener for each opportunity. Also, the small firms (500 employees or less) appear to be able to make use of twice as many (proportionately) managerial personnel as the very large firms (5,000 employees or more). The ratio for the small firms is about 1 manager to 5 nonmanagers, whereas this ratio in the very large firms is only 1 to 10. There

must be basic profit and cost characteristics which result from this wide difference in managerial emphasis.

Another basic point of interest is the wide range of individual differences which exists for firms of the same size and type. Although the trends overshadow these variations, the reasons for such differences, and the relation of these variations to profit figures should be studied further. Controlled research should be able to define the most profitable and effective managerial ratio for each type and size of business. Valid information of this kind could be of great practical value for American businessmen. There are many other implications, but it is not the purpose of this study to go beyond the broader aspects of the problem.

One other index was computed, but

since the findings were negative they were not reported in detail. There has been considerable discussion in recent years of the relationship between profit and organizational structure. With this in mind, 1951 profit figures before taxes were obtained for about half of the firms studied, and these were correlated with the percentage of total managerial personnel in each business. The results obtained indicate that no relationship exists. If a larger sample were used so that breakdowns could be made by type or size of business, some relationship—positive or negative—might be discovered.

The findings of the study indicate that further work should be carried out to document and expand this pilot investigation.



# Financial Reporting and Business Decisions

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THROUGHOUT the life of an enterprise its management is faced with a continuing series of decisions with respect to financial matters. During periods of financial stress, such decisions loom large and receive considerable attention. At other times, particularly when management finds other matters such as production, sales, or the acquisition of additional facilities demanding more attention, financing may receive less than its just share of managerial consideration. Yet the importance to a business enterprise of individual financial transactions and of financing in general is such that they deserve the careful and informed attention of management at all times.

Financial decisions may be looked on as divisible into two groups. For purposes of discussion here, these may be called "conscious" and "unconscious" decisions. To suggest that management makes unconscious decisions on financial matters may appear a bit harsh, yet in many instances that is a reasonable description of what takes place. Let us contrast two situations. Assume first a situation in which a given concern is in need of funds for expansion. After full discussion in meetings of the board of directors, its officers are authorized to go into the market and arrange to obtain funds from whatever source they find most economical in view of all pertinent considerations. Assume further that management, after due deliberation, determines that an

issue of 5 percent preferred stock constitutes the most desirable source of the needed funds and goes into the market with such an issue. This certainly represents a conscious decision and, in line with our assumptions, is one made in view of all available facts.

Now let us assume a somewhat different situation, one in which a concern has an outstanding issue of 5 percent bonds. Let us also assume that credit conditions and interest rates have changed to such an extent that money can now be borrowed under similar terms for as low as 4 percent. In a vague sort of way, management of this second enterprise is aware of a general change in credit conditions, but because no specific event has related this general condition to its own financing position, it fails either to see or to act upon the opportunity. Because it does not act, it has in effect made a decision by default, a quite unconscious decision to continue financing with 5 percent bonds when it could profitably have refunded with 4 percent bonds.

Of course all situations are not so clear-cut as this. The derelictions of management are not always so apparent — which is one of the reasons they occur. Yet apparent or not, it is safe to assume that they do take place and that they may be costly to the enterprise concerned. Over a long period of time, an accumulation of decisions of this nature could be disastrous.

Accountants as a group must take

their share of the responsibility for unconscious managerial decisions on financial matters. Although they have generally done a reasonably good job of bringing important information to the attention of management (in balance sheets, income statements, cash reports, budgets, and progress reports on construction programs), very little has been done with reports on financial activities. This area of enterprise activity has not received the attention it deserves, and as a result, management is not as fully informed as it might otherwise be. Thus financial decisions are likely to be made by default or on the basis of inadequate information.

To be in position to make consciously and intelligently the decisions with regard to financial matters that face it daily, management must have available the answers to such questions as these:

- (1) What types of financing do we now have in effect and what is the extent and cost of each?
- (2) What is the relative importance of each to the enterprise?
- (3) Which types tend to fluctuate throughout the year and therefore require constant attention (i.e., to meet seasonal needs), and which remain relatively constant?
- (4) Historically, has there been any tendency to shift from one type of financing to another, and if so, do present conditions justify maintaining that trend?
- (5) In view of current interest rates and other conditions of the money market, are modifications of the existing financing plan in order?

In addition, sound financial policy requires that management give attention to a wide variety of considerations. Among them are (1) a constant review of the desirability of alternative methods of obtaining financing, (2) alertness to possible or potential transactions favorable to the company, and (3) maintenance of an appropriate balance or relationship among the various financing interests. Well-organized reports of financial transactions provide management with some of the information it needs to answer these questions and with a means of keeping constantly before it a reminder of some of the most important problems of maintaining a sound financing program.

Generally accepted practice calls for an income statement to report on operations or profit-directed transactions, a balance sheet to report on financial condition, and a surplus statement to reconcile the two. Careful study of the content of these reports shows that they omit financing transactions. They do not present data on the activities of the enterprise directed toward obtaining and repaying the funds required for operating purposes.

### **Complementary Statements Helpful**

It is not because information is unavailable or difficult to obtain that adequate data on financing activities are omitted from accounting statements in current use. Reports of financial activities can be prepared from any ordinary, well-kept, double-entry set of accounts. No new records need be kept and no new procedures are necessary. The essential information is all present within the regular ledger accounts; it need only be extracted and arranged.

Illustration I  
ILLINOIS MANUFACTURING COMPANY  
STATEMENT OF FINANCING  
For the year ended December 31, 1951

	Financing Provided			Cost of Financing Provided	Ratio of Cost to Average Financing
	Jan. 1, 1951	Dec. 31, 1951	Average		
Primary financing interests					
Banks.....	\$ 100,000	\$ 450,000	\$ 173,333	\$10,400	6.00%
Bondholders.....	-0-	480,750	360,312	21,375	5.93
Preference shareholders....	500,000		166,667	17,500	10.50
Common shareholders.....	1,468,000	1,613,700	1,529,900	48,000	3.14
Total.....	<u>\$2,068,000</u>	<u>\$2,544,450</u>	<u>\$2,230,212</u>	<u>\$97,275</u>	4.36
Incidental financing interests					
Trade creditors.....	\$ 320,000	\$ 768,600	\$ 530,877	-0-	
Accrued expenses.....	42,000	47,000	44,800	-0-	
Total.....	<u>\$ 362,000</u>	<u>\$ 815,600</u>	<u>\$ 575,677</u>	<u>-0-</u>	
Total financing.....	<u>\$2,430,000</u>	<u>\$3,360,050</u>	<u>\$2,805,889</u>	<u>\$97,275</u>	3.47
Nonfinancing interests					
Federal income taxes.....	381,000	137,000			
Total interests.....	<u>\$2,811,000</u>	<u>\$3,497,050</u>			

Illustrations I and II show the types of possible reports. They present useful financial information not now made available in the financial statements which are generally used.

Illustration I, which ties in with the credit side of the balance sheet at the beginning and at the end of each period, directs attention to the types of financing in use and to the extent and cost of each. By showing the relative cost of each method, it raises a question as to the desirability of shifting from one method to another. A series of such reports over a period of years would reveal any tendency to favor one method of financing over another. To anyone with a knowledge of credit conditions in general and the company's financial policy in particular, it provides a basis for evaluating the soundness of the policy and the extent to which the policy is followed.

Illustration II, the statement of enterprise growth, presents a further aspect of the financial transactions through which an enterprise grows or decreases in size. Borrowing, issuance of capital stock, and retention of earnings are the means by which a firm adds to its total assets and thus to its size. Reversal of these transactions distributes assets and reduces the size of the concern. A complete report of amounts obtained from the various interests in the enterprise and repaid to them portrays the means by which the enterprise grew or diminished during the period. This report points up a feature of enterprise success not indicated in the customary accounting reports.

If reports such as those illustrated were regularly presented to management, it seems likely that more managerial attention would be given to the



## Illustration II\*

## ILLINOIS MANUFACTURING COMPANY

## STATEMENT OF ENTERPRISE GROWTH

For the year ended December 31, 1951

## Increases in enterprise properties resulted from

## Advances by

Trade creditors.....	\$4,008,500		
Employees.....	1,609,700		
Banks.....	580,000		
Bondholders.....	480,000	\$6,678,200	

## Income from operations

Net income accruing to common shareholders..... \$ 221,200

## Claimed by taxing authorities

Federal income tax.....	\$137,000		
Other taxes.....	55,800	192,800	

## Claimed by creditors as interest

On bank loans.....	\$ 10,400		
On bonds.....	21,375	31,775	445,775

Total increases..... \$7,123,975

## Decreases in enterprise properties resulted from

## Discharge of obligations to

Trade creditors.....	\$3,568,775		
Employees.....	1,605,700		
Banks.....	230,000		
Preference shareholders.....	510,000	\$5,914,475	

## Payments for use of assets advanced

## As interest

On bank loans.....	\$ 6,900		
On bonds.....	13,750	\$ 20,650	

## As dividends

On preferred stock.....	\$17,500		
On common stock.....	48,000	65,500	86,150

## Payments to taxing authorities

Federal income tax.....	\$ 381,000		
Other tax.....	56,300	437,300	

Total decreases..... 6,437,925

Net enterprise growth..... \$ 686,050

\* A complete discussion of methods for the preparation of these reports may be found in Robert K. Mautz, *An Accounting Technique for Reporting Financial Transactions* (Urbana: Bureau of Economic and Business Research, 1951).

problem of financing enterprise activities and that unconscious decisions might be less frequent.

Reports such as these have other benefits as well. In addition to directing the attention of management to financial operations as an important phase of enterprise activities, they also (1) furnish a basis on which stockholders and creditors can evaluate the judgment and success with which man-

agement meets financial problems, much as the income statement provides a basis for appraising managerial efforts in operating matters; (2) supply an important link in budgetary procedure to correlate financing with operating needs; (3) facilitate an understanding of the nature of the various enterprise interests and their contribution to the business; and (4) provide a measure of enterprise

growth and data pertaining thereto which is useful not only to management but in the general area of economic analysis as well.

### *1. Reports to Stockholders and Creditors*

Stockholders, creditors, and other interests in an enterprise necessarily place a considerable trust in management. To determine at reasonable intervals whether or not that trust is warranted, these interests require information as to managerial decisions taken and their results. Financial statements have often been described as reports by management of its stewardship over the assets advanced to the company by the various interests in the enterprise. Some of the most important decisions made by management in discharging its stewardship are found in the area of financial transactions. Yet no adequate report of such activities is now made available to stockholders and creditors. Some information on this subject can be gleaned from the income statement and the balance sheet, but only a very limited amount. Also, such information as is available in those reports is not presented in such a way as to give an organized, integrated picture of this area of managerial effort. The reader of an annual report now has little basis for evaluating the success with which management has handled financial matters during the year under review.

Surely stockholder and creditor interests in an enterprise are entitled to such information. If they are to act intelligently in advancing or withholding funds from the enterprise, they must have some basis for appraising all important managerial decisions. They too

must decide whether possible financial transactions appear desirable, whether present financing is too costly in view of the alternatives, and whether opportunities for such activities as trading on the equity have been overlooked. Only if they have adequate information to arrive at answers to such questions are they able to judge on a sound basis the efficiency of financial management. Full disclosure of financial transactions through organized reports helps give them such information.

### *2. Link in Budgetary Procedures*

The relationship to budgeting of reports such as the ones mentioned here is probably so apparent that little comment is required. Useful budgetary procedures require, together with other information, the anticipation of cash receipts and disbursements for some period in advance. Statements of financial transactions should be helpful in this respect in that they present for review the various obligations of the company as well as opportunities for obtaining additional funds. Full information on maturing obligations, whether they are short-term or long-term, is readily available in these reports. Further, because each obligation is presented as one part of the over-all picture of enterprise financing, methods of replacing any funds required for the discharge of maturing debts, assuming that is considered desirable, are suggested almost as a matter of course.

### *3. Aid to Understanding the Nature of the Various Interests*

The balance sheet is of limited value in understanding the nature of the various interests in an enterprise since it shows them merely as obligations to

be met by the enterprise out of its resources. This had led to classification of such obligations into creditorship interests, those to be repaid, and ownership interests, those which have advanced funds to the enterprise for periods so indefinite that the advance appears permanent. Over the years, new combinations of the rights and privileges attaching to these different interests have tended to make less clear the traditional difference between these two types of corporate equity. This has made the problem of balance sheet reporting more difficult, and therefore the problem of understanding the nature of the interests in the enterprise has become more difficult also.

In contrast, a statement of financing reports the interests in the enterprise from quite another viewpoint. In this report, all interests are providers of financing. This characteristic they all have in common: each one supplies the enterprise with assets. Some provide financing for longer terms than others, but inasmuch as the enterprise does hold assets claimed by the various interests, all may be considered to be financing the company. Each therefore contributes something to the enterprise; each is a factor in its expansion or contraction. Some of these interests charge a fee for the financing that they provide; others do not. This leads to a consideration of the extent of the financing provided by each interest, the relative cost and the desirability of various types of financing, and of course the other features of the arrangement between the company and each interest so that a complete understanding of the relationship may be obtained.

#### *4. Measure of Growth*

The success of an enterprise may be looked on as composed of three features: maintenance of a sound financial position, realization of an adequate return on invested capital, and expansion or contraction in accordance with the plans and desires of its management. Financial condition and profits are presented in the balance sheet and income statement, respectively; we do not, however, have a report to show the extent and nature of enterprise growth during the fiscal period. If the success of the enterprise is to be judged adequately either by its management or by other interests in the enterprise, it seems that some information as to whether or not the firm is growing and precisely how this is being accomplished should be made available to them. Illustration II shows a report which brings together the various components of enterprise growth, the increases and decreases in enterprise properties. Full disclosure certainly implies some attention to this important aspect of successful operations.

Recent years have seen an increased use of enterprise accounting data by various interests outside the specific companies to which the data apply. Government planners and large-scale business planners alike have found it helpful to have as much information as possible about business activities. Whether they are concerned with the estimation of national income by government or with the estimation of the possible demand for a product by a large industrial concern, reliable indications as to the growth of individual firms in the area of interest may be very helpful. Growth, both of our economy



as a whole and of individual units or segments of it, is becoming more and more a subject of interest and consequence. Reports of enterprise growth can provide both a measure and an explanation of this significant economic phenomenon.

### Conclusion

As with any new report, there is some danger that too much will be expected. That the suggested statements are useful seems apparent. They direct attention toward an important and perhaps neglected area of managerial effort and provide a basis for the evaluation of managerial accomplishments in the field of financial activity. They also help us understand and control enterprise activities. However, the proposed reports do not provide a panacea for financial problems and difficulties. They are but a means to solutions; they are not solutions in themselves. Certainly careful study of their content is required. Integration with the informa-

tion presented in other reports and the recognition of relationships through the use of ratios and other interpretive devices should be helpful and even necessary if full benefit is to be realized.

Finally, it should be noted that the addition of these reports to those already in use does not yet provide a complete disclosure of enterprise activities. Certain types of transaction such as the equal exchange of one asset for another (collection of receivables, purchase of fixed assets, or purchase of securities and sale thereof if not at a gain or loss) and conversions of assets within the manufacturing process, to cite but two examples, are included in neither the income statement nor the proposed statements of financing. We still fall short of full disclosure of all enterprise transactions, but we come considerably closer to this goal with the addition of statements reporting financial transactions than we do without them.

# Packer Reservation Prices and Price Discovery in the Wholesale Pork Market\*

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THE concept of *reserve* or *reservation* prices is introduced to students early in the study of economics. Usual practice calls for a definition, but from this point on little use is made of it. The reservation prices represent prices at which the firm will keep the product rather than sell it. How are such prices formed? What effect do they have on individual firms, on prices, and on product distribution throughout the marketing season? This paper examines the nature and significance of packer reservation prices on pork products.

## Packer Reservation Prices

The actual quantities of product that a slaughtering plant makes available to wholesale buyers at various prices in any one time period depends on the quantity of product on hand, the

quantity produced, and the firm's reservation prices.<sup>1</sup>

The reservation prices do not usually apply to the total supply of products on hand, but to the "excess supply."<sup>2</sup> Most firms ordinarily will sell a minimum amount of product at whatever market price prevails in order to supply their best or regular customers. Once a retail sales territory has been developed, firms are extremely reluctant to take any step, such as the refusal to supply the customer with product at existing market prices, which may result in loss of the customer.

Packers thus tend to sell whatever minimum quantity they need to in order to maintain present customers and keep their distributive organization operating. Actually this results in a maximization of returns over the long run. Most firms find that it is best to sell some product at all times at whatever prices exist. Such action will maintain customers and reduce the per unit overhead costs of maintaining the distributive sales organization.

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\* This article is based on a survey-study of the actions of nine hog-slaughtering firms. The study was made between October, 1951, and May, 1952. The nine firms annually slaughter about one-fifth of the total production of hogs in the United States. They range in size from small commercial plants to very large multiple-plant firms. Further information regarding the sample and techniques will be supplied upon request.

The range in size of firms, the variations in types of operations, and the small size of the sample make it necessary to present the data in a hypothetical form in order to prevent identification of the practices discussed with individual cooperating firms.

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<sup>1</sup> A "firm" refers to a business organization under one management whose operations include the slaughtering of hogs and the processing and distribution of pork products.

<sup>2</sup> The term "excess supply" refers to that portion of production which is over and above the minimum needed for a firm's own processing requirements and regular customers.

## Derivation of Total Demand Schedule for Pork Loins at Wholesale

Loin price (\$ per cwt.)	Total demand for consumption	Demand for storage						Total demand schedule
		Firm A	Firm B	Firm C	Firm D	Other <sup>a</sup>	Total	
100	300							300
95	310							310
90	320							320
85	331							331
80	342							342
75	357							357
70	371							371
65	388							388
60	406							406
55	428							428
50	452							452
45	480							480
44	487					5	5	492
43	494	5			1	5	11	505
42	501	5			1	5	11	512
41	510	5			5	18	28	538
40	516	5		10	5	24	44	560
39	523	10		10	5	44	69	592
38	532	10		20	5	63	98	630
37	541	20		20	10	109	159	700
36	550	20	40	30	10	180	280	830
35	560	50	40	30	10	190	320	880
34	570	50	40	30	10	210	340	910
33	580	50	40	30	10	226	356	936
32	590	50	40	30	10	230	360	950
31	600	50	40	30	10	231	361	961
30	611	50	40	30	10	231	361	972
25	681							
20	778							
15	920							

<sup>a</sup> Includes holdings by other slaughtering firms, nonslaughtering processors, and purely speculative interests. Does not include minimum inventory requirements or demand for storage by consumers.

The level of reservation prices established on excess products depends on several factors. The firm's estimate of future price conditions is a primary factor. Price expectations both in the live hog market and in the pork product market are involved.

When a firm expects the price of live hogs in the immediate period ahead to be lower than at present, the reservation price will tend to be lower than if steady or higher live hog prices are anticipated.

If the firm expects product prices to decrease in the period ahead, the reservation

price will be low. If higher product prices are anticipated, then the reservation price will be high.

Some packers' reservation prices are influenced by their need for cash. If their credit is not of high order, banks may not lend them money to hold inventories or they may even be pressing for payment of old obligations. Under these circumstances firms cannot afford to have money tied up in inventories and will be eager to sell as quickly as possible. Their reservation prices will then be lower than if these firms were not pressed for cash.



Some packers develop one reservation price for pork products. They attempt to sell all excess production above this price but store that which cannot be sold at the reservation price. Some tend to think in terms of one reservation price for the whole of the excess production but graduate sales so that in actuality there are reservation prices for different portions of the excess production.

Other packers have different reservation prices, as illustrated in the accompanying table. For example, firm C will store ten units of loins at one price, 20 units at a lower price, and 30 units at a still lower price.

There are several reasons for having different reservation prices. The amount of cold storage facilities owned or otherwise readily available to a firm is a factor in the decision. For example, a packer might be willing to sell at a low price the quantity in excess of that for which he has readily available storage space. In fact, he may be forced to sell it. However, it would take a higher price to induce him to sell that part of the excess production which can be conveniently stored.

A packer may also have a different price for products that can be further processed by his own firm. For example, one firm may have a well-established trade outlet for hams. This firm will have a high reservation price for the hams needed to meet its own processing requirements in the planning period ahead. It will take a higher price to induce the firm to part with that portion of the current excess production (hams in this case) which can be used later than it would take for

the excess production that will not be needed for processing later.

Past cost should have no influence on the current sale price or on the reservation price of a perishable commodity; yet some firms permit cost price to influence their reservation prices. One firm, for example, reported that it will not sell canned hams when the market price drops below what it cost to produce the hams.

The establishment of rigid reservation prices on a cost of production basis makes the firm extremely vulnerable to loss in case of price declines. It can be particularly disastrous in a year of sharp decline or in a series of years in which the price trend is downward.

The ability of business leaders to decide when it is best to take a loss on inventories in order to avoid greater loss later is an important key to successful inventory management.

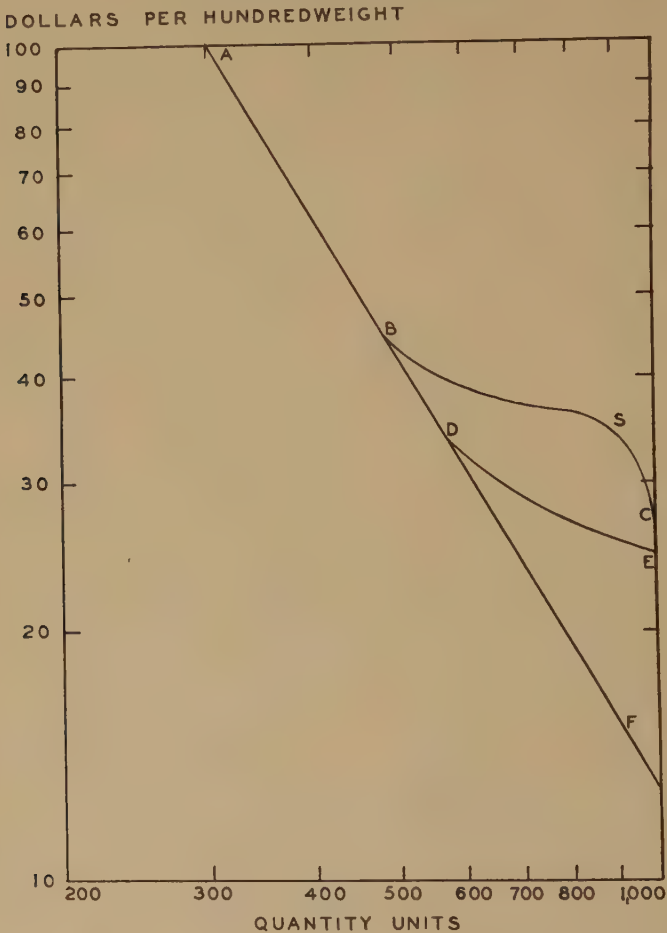
### **The Reservation Price and Price Discovery in the Wholesale Meat Market**

Those interested in the nature of price discovery in the market place will find price making in the wholesale pork market an interesting area of speculation. We shall use pork loins in this treatment of price discovery.

The only time period that packers are concerned with is short-run in nature and a period in which a near-fixed supply condition exists. Let us consider price making in the three months of heavy market receipts—November, December, and January.

There are several specific categories of persons desiring to own pork loins—consumers (whose demand is reflected

### Hypothetical Illustration of the Effect of Packer Reservation Prices on the Demand for Pork Loins



through those who buy in the wholesale market for retail and food service sales), nonslaughtering processors, pure speculators,<sup>3</sup> and slaughtering firms. Consumers and slaughtering firms account for most of the desire to own pork loins.

<sup>3</sup> "Pure speculators" are those individuals who are neither slaughterers, processors, nor wholesale dealers in pork. They buy or sell pork only for the purpose of taking risks in the hope of making a speculative gain.

An assumed schedule of quantities retail buyers will take (for consumers) at specific prices is shown in the table and illustrated graphically by the line AF in the accompanying chart. The storage demand for pork loins stems from the packers who slaughter the hogs, nonslaughtering processors, wholesale buyers, food chains, and those who buy and store purely for the

purpose of assuming risk in anticipation of a speculative return.<sup>4</sup>

The major proportion of the demand for storage comes from the slaughterers. Some examples of packer demand for storage are indicated in the table under hypothetical firms A through D. These examples were prepared to indicate the type of reservation prices observed in the course of the study. The total production for firms A and B in the time period examined is assumed to be 150 units each. A production of 100 units each is assumed for firms C and D. Maximum pork loins production in the time period examined is assumed to be 1,000 units.

Every firm must hold a certain proportion of its product in inventory as long as it is in operation. This inventory base expands and contracts seasonally with hog production as the volume of plant operations varies. Thus, some of the inventory accumulated in the November-January period is necessary to fill the pipe lines as the firm moves to a higher volume level.

<sup>4</sup> In a market in which the supply of a commodity is fixed for a given period, it is valid and often useful to combine the demand of purchasers (retailers) of the product with the demand of suppliers to hold the product in storage. Combination of these two types of demand involves, in a sense, a combination of the demand curve with the supply curve. In the words of Wicksteed, "When we are speaking of a marketable commodity, what is usually called a supply curve is in reality the demand curve of those who possess the commodity; for it shows the exact place which every successive unit of the commodity holds in their relative scale of estimates." Philip H. Wicksteed, "The Scope and Method of Political Economy," *Readings in Price Theory* (Chicago: Richard D. Irwin, Inc., 1952), pp. 15-19.

This kind of inventory increase is of the unintentional or involuntary type and is not considered in this example of price discovery. The involuntary inventories have no appreciable influence on the market price level. The figures for the different firms in the table represent that demand for inventory which is above the minimum involuntary accumulation.

It will be noted in the example firms that there are from one to four critical points where the quantity of pork loins stored changes. This is fairly typical of most firms.

Firm A illustrates several critical points. At these points a shift in inventory policy occurs. Firm A will store some loins at \$43 per hundredweight. The quantity stored increases when the price drops to \$39. Further increases in the quantity stored occur as loin prices decrease to \$37 and to \$35.

Some firms start accumulating inventories at one certain price. For example, firm B does not choose to accumulate pork loins until the price drops to \$36 per hundredweight. If they cannot get this price, firm B will store all production in excess of the amount which must be sold to regular customers in order to keep them satisfied and to keep the sales and distribution organization at an optimum operation level.

The addition of the demand for consumption and the demand for storage illustrated in the table yields a curve with a rather flattened area where the demand for storage is expressed. Then it breaks off sharply. This is illustrated by the curve ABSC in the chart. The line AF represents the assumed total



demand for consumption. When the total demand for storage is added to this curve, the result yields the curve ABSC. The curve begins to flatten at point B, where some firms will store pork. The rapidity with which this curve levels out depends on the range and nature of the distribution of reservation prices.

There is some point, S, on this price-quantity curve where a limitation on storage space is reached. Beyond this point the price must drop sharply in order to move additional production into consumption. Pork must compete with other foods for cold storage space and there is a practical limit on the space available. Such a point was actually reached in the early months of 1952. Most of the regularly available space was leased by mid-November. It became difficult to find space as the slaughter season progressed and the point was reached where many packers could not find space. They then faced the problem of moving the total current production into consumption when the freezer space they owned, or had leased, was filled.

The low level of wholesale pork prices (and live hog prices) in February, 1952, may be directly attributed to this freezer space shortage. This should not be misinterpreted by the trade as an indication that there is insufficient storage space. Actually, storage stocks were at a very high level compared with other years, indicating that reservation prices were established too high to be maintained throughout the season of heavy slaughter. They were too high to permit pork to be

stored on a sound economic basis or to permit the stabilization of hog and pork product prices through an adequate storage holding program.

What would be the effect of packers establishing reservation prices at a different level? What if packers had less confidence in pork prices than assumed above?

Let us assume that firms in the industry established reservation prices at a level \$10 lower than that discussed above. The price-quantity curve illustrated by ADE then results. This curve exhibits a quite different elasticity. When maximum production does not exceed 1,000 units (as assumed above) the lower packer reservation prices have the effect of making the lower end of the curve more elastic. The point is not reached where storage space is limited, and the resultant sharp decrease in elasticity does not occur as in the SC section of the curve ABSC.

The price of pork loins will be established where quantity plotted corresponds with the total aggregate demand curve.

What happens if the industry establishes average reservation prices at too high a level? If the industry is overly optimistic and sets its schedule of reservation prices too high, then a sharp break in pork prices develops at the time that this becomes apparent or when the physical limitation is reached on the quantity of pork that can be stored.

More pork is consumed currently and less is stored for future consumption when reservation prices are low than when they are high. If the reser-

vation price for pork loins is established too low during the heavy slaughter season, an insufficient quantity is accumulated for consumption in the periods of seasonally low production.

Large firms must be extremely careful in establishing reservation prices. Take firm A, for example, with a total production of 150 units out of the 1,000 units maximum production. If firm A stores one-third of its production during the heavy slaughter period, this represents 5 percent of the total production. This can have a substantial effect on current market prices. Thus the large firm, by starting inventory accumulation at a certain reservation price, may cause the market price to indicate strength. The strength registered in the market may easily lead this firm (and perhaps other firms) into feeling overoptimistic in the very short run.

Smaller firms frequently follow the storage practices of larger firms. In other words, they may start accumulating inventories when some large firm starts. They reason that the larger firms have more research funds and can do a more extensive job of market analysis and know better when to store pork products.

Exception is frequent, however, since there are many persons in the market who think they can judge markets better than the larger firms. They will continue to sell pork and try to take customers from the firm or firms which are storing part of their production. If these persons' estimates of the market are correct, they will succeed in gaining competitive advantages. They

might even do serious damage to the large competitor by taking some of the large competitors' regular customers.

How do the small firms know what the large firms are doing? This is generally easy to find out. Even though large firms are cautious and secretive about plans, their market operations are known. This information spreads rapidly through brokers and other market interests. For example, if firm A starts accumulating its excess production instead of selling it, word quickly spreads through brokers that firm A will not sell loins below such-and-such a price. If other market interests also think that this looks like a good point to start storing, they may follow suit.

No one firm in the packing industry can control supplies. Even though the actions of large firms in the market may be followed temporarily by competitors, these competitors are ready to make independent decisions whenever, in their opinion, economic conditions justify it. In other words, large firms can be successful leaders in a market action *only* so long as their actions are correct, and *only* when they are the first to anticipate the correct actions and changes to make in order to achieve a market equilibrium.

### Summary

This treatment of reservation prices has been simplified somewhat in comparison with the actualities of the market in the interest of clarity. As a practical matter, reservation prices and inventory plans of most firms are flexible and subject to change from day to day or from week to week as market

demand and supply conditions and market expectations change.

The demand by packers for pork for storage is reflected in their reservation prices. Firms must be careful in establishing reservation prices. If the reservation price is above that justified in the market, then they may lose custom-

ers and find themselves faced with large and undesired inventories. A reservation price that is too low may lead to unnecessary operating losses (or smaller profits than necessary) and to a shortage of product for their own processing requirements later.



# The 1952 Coal Settlement

JOHN A. COCHRAN

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THIS year, once again, three parties have been involved in shaping the terms of the final settlement in coal. Not only did the two major coal operator associations bargain with the miners' union over the terms of a new contract, but as has happened so often in the past, the government intervened to influence the outcome. Usually the Federal government interjects its offices into a coal dispute in an effort to secure an agreement between the operators and the union. This year management and labor had already reached a contract settlement to find that only \$1.50 of the scheduled \$1.90-a-day wage hike would be permitted by the Wage Stabilization Board under its interpretation of national stabilization policy. This decision on October 18 precipitated a full-scale miners' walkout on October 20. The walkout was ended one week later after President Truman, at a special White House meeting, prevailed on John L. Lewis to order his miners back to work. No government decision on Lewis's demands for the full wage hike was to be rendered until after the election on November 4. A month after the election, President Truman announced his personal decision to allow the full wage increase of \$1.90 per day. What were the developments which led up to the 1952 coal settlement?

## The Competitive Position of Coal

Any discussion of the coal industry, whether of prices to the consumer or

of wages to the miners, ultimately comes down to a discussion of the position of coal in relation to its market competitors—fuel oil and gas. The ability of the industry to pay higher wages, or the effects of such higher wages, must always be viewed in this market nexus of coal and its rivals.

The position of coal in 1952 in relation to its competitors is not very favorable. Coal has been steadily losing out over a number of years in the proportion of total energy consumption which it supplies. This long-term trend has been accelerated, if anything, in recent years. Over a period of 31 years, coal has greatly declined in relative importance, as is indicated by the fact that whereas it furnished nearly three-fourths of total energy requirements in the United States in 1920, the proportion in 1951 was less than one-half. The accompanying table shows this decline and also indicates its cause. For during this same 31-year period, petroleum products increased their share of the fuel market from a low figure of 7.0 percent to a high of 24.0 percent and natural gas boosted its share from 4.3 percent to 23.9 percent. These two competitors of coal together supplied a greater amount of energy requirements in 1951 than did coal, though in 1920 their combined percentage was only one-seventh that of coal. Part of this trend is to be attributed to technological changes which have opened up new utilizations of energy best satisfied by

## Coal and Other Energy Consumption in the United States, 1920-1951

Year	Bituminous coal consumption (000 tons)	Percent of total on Btu basis				
		Bituminous	Anthracite	Petroleum products	Natural gas	Hydro-electric
1920.....	508,149	71.8	11.7	7.0	4.3	5.2
1921.....	391,027	67.7	13.8	8.9	4.2	5.4
1922.....	427,099	70.6	9.1	10.4	4.7	5.2
1923.....	516,944	69.7	11.4	9.5	4.9	4.5
1924.....	483,631	68.3	11.1	10.7	5.6	4.3
1925.....	498,159	70.1	8.7	11.1	5.9	4.2
1926.....	531,083	68.9	9.7	11.0	6.2	4.2
1927.....	498,677	67.3	9.8	11.4	7.0	4.5
1928.....	499,622	66.6	9.5	11.7	7.5	4.7
1929.....	519,117	66.5	8.9	11.8	8.5	4.3
1930.....	452,639	64.0	9.3	13.0	9.5	4.2
1931.....	373,736	62.5	9.5	13.7	10.0	4.3
1932.....	309,161	59.7	9.5	14.7	10.7	5.4
1933.....	321,178	60.5	9.1	14.8	10.3	5.3
1934.....	345,762	60.3	9.4	14.8	10.7	4.8
1935.....	360,898	59.9	8.2	15.5	11.1	5.3
1936.....	420,796	61.5	7.5	15.3	11.0	4.7
1937.....	428,957	60.5	6.9	15.8	11.6	5.2
1938.....	343,345	56.6	7.2	17.3	13.0	5.9
1939.....	379,910	57.2	7.3	17.5	12.8	5.2
1940.....	439,252	59.2	6.4	17.2	12.3	4.9
1941.....	480,988	59.4	6.3	17.4	12.1	4.8
1942.....	537,885	59.9	6.1	16.7	12.1	5.2
1943.....	593,697	59.4	5.5	17.3	12.4	5.4
1944.....	594,186	57.8	5.6	18.4	13.0	5.2
1945.....	563,307	56.1	5.0	19.3	13.9	5.7
1946.....	488,891	52.9	5.7	20.1	15.3	6.0
1947.....	557,405	54.2	4.5	20.4	15.4	5.5
1948.....	534,265	51.4	4.7	21.2	17.2	5.5
1949.....	440,195	46.7	3.9	22.7	20.3	6.4
1950.....	458,018	44.5	3.7	23.9	21.9	6.0
1951 Prelim.....	476,013	43.3	3.3	24.0	23.9	5.5

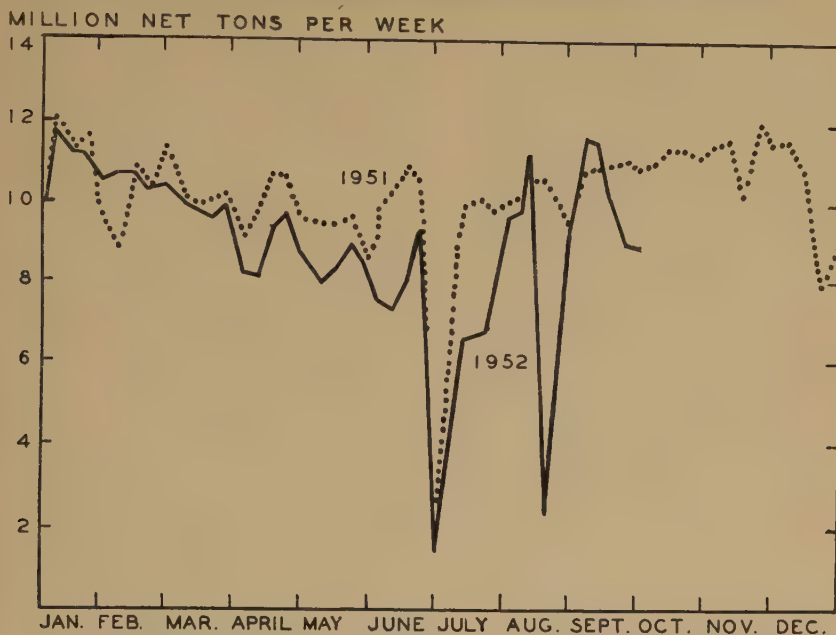
Source: From data in Bituminous Coal Institute, *1952 Bituminous Coal Annual*, p. 9.

fuel oil or natural gas. However, another important part of the story is to be found in the invasion of the traditional markets of coal by these aggressive new competitors. As one can see in the table there has been a secular decline in total coal production. This declining trend, which has continued in the postwar period, has gone hand in hand with a decrease in coal con-

sumption from 508 million tons in 1920 to 476 million tons in 1951. These facts form the statistical basis for the often-heard assertion that soft coal mining is a declining industry.

Even comparing this year with last, and using production figures rather than consumption figures, one can gain some idea of the competitive plight faced by the bituminous coal industry.

## Production of Bituminous Coal and Lignite in 1951 and 1952



Source: Bureau of Mines, *Weekly Coal Report for October 17, 1952*.

In the accompanying chart, 1952 coal production through the week ended October 11 is compared with production during 1951. Even disregarding the unusual dip in production in late August and early September caused by the special memorial period called by Lewis, it is obvious that production is less this year than it was last year. Despite a higher level of industrial activity, total soft coal production this year to October 11 was only 363,260,000 tons as compared with output of 411,692,000 tons up to October 13 of last year. This represents a decline of 11.8 percent in production.

Even the demonstrated decline in production does not completely represent the competitive losses coal has suffered this year, since coal stocks rose

from 70 million tons in January to over 80 million tons in July.<sup>1</sup> (This represented 80 days of normal consumption of coal.) If further evidence is needed of the competitive difficulties of coal, it can be found in the fact that markets for coal have been so soft this year that most companies have been selling coal 65 or 70 cents below their price ceilings.<sup>2</sup>

The coal operators tried to raise prices about 25 cents a ton after they gave the miners a wage increase of \$1.60 a day in January, 1951. But soon coal prices had drifted even lower than they had been before the wage settlement. And it is not only the competi-

<sup>1</sup> Bureau of Mines, *Weekly Coal Report for September 5, 1952*.

<sup>2</sup> *New York Times*, June 15, 1952.



tion from other fuels which the union operators must fear. Competition from nonunion mines in Ohio, West Kentucky, and Central Pennsylvania has sharpened the downward pull on prices. Some of these nonunion mines have been offering coal at prices as much as \$1 lower than those charged by union mines. The profit margin per ton of coal which was, on the average, 40 to 45 cents a ton in 1951 is less than half that this year, according to some industry experts. The immediate future outlook for coal is not much better, since some pessimistic industry forecasts predict a decline in annual coal production to a low point of 400 million tons in 1954. (This compares with a peak production of 630 million tons in 1947.) Some of these same forecasters see a sharp upward swing in the demand for coal after 1960 as a result of electric power demands and new uses for coal.<sup>3</sup>

### The Bituminous Coal Operators Association

In the face of increasingly tough competition for coal in the energy market, coal operators had become particularly sensitive to any further loss of markets. However, price and convenience of use of other fuels (for domestic users) were not the only problems with which they had to contend. Many of coal's regular customers were unhappy about the annual threat of a coal strike with the consequent threat to the continuity of coal supplies. Part of the 80-million-ton coal stockpile can be attributed to the desire on the part of coal users to have some security

of continued production if the supply of coal from the tipples is interrupted by a strike. But even huge stockpiles will eventually be consumed if the strike drags on long enough, and the actual occurrence of a strike is likely to force the large industrial consumers of coal to institute some production slowdowns after a while in order to conserve their dwindling stockpiles.

Hence, a direct attack on the problem of the periodic coal strike naturally came to mind. To that end a new association of coal operators under the leadership of the captive-mine owners and large northern commercial operators was formed in 1950, after the conclusion of the long-drawn-out strike of 1949-50, to present a more united front in bargaining with Lewis and the United Mine Workers and to attempt to secure a greater stability of labor relations in coal so as to prevent the periodic interruptions in the supply of coal.

This new organization, which was called the Bituminous Coal Operators Association, was activated on October 1, 1950, with headquarters in Washington, D.C. Harry Moses, who had been president of H. C. Frick Coke Company (coal subsidiary of U.S. Steel) for 13 years, was chosen as president of this new operators' bargaining group. Coal operators with approximately 153 million tons of bituminous production were represented in the new association. The mines owned by these companies were located in Pennsylvania, Ohio, West Virginia, Virginia, and Kentucky.<sup>4</sup> In addition to this new

<sup>3</sup> *Ibid.*

<sup>4</sup> *United Mine Workers Journal*, October 1, 1950.

bargaining association of Appalachian coal field operators, there was already in existence the Southern Coal Producers Association headed by Joseph E. Moody and representing some 100 million tons of southern coal production.

This new organizational alignment on the operators' side proved to be quite important in the 1952 coal negotiations since it was with the Bituminous Coal Operators Association that the United Mine Workers reached the agreement which would become the pattern for the entire industry.

### Union Strategy in the Negotiations

The National Bituminous Coal Wage Agreement of 1950 as Amended January 18, 1951, provided that "either the parties of the first part or the party of the second part may, on or after March 31st, 1952, terminate this Agreement by giving at least sixty (60) days' written notice to the other party of such desired termination date." Thus the party of the second part, the United Mine Workers, could have given notice of the termination of agreement on February 1, 1952. Lewis did not, however, choose to exercise his option at this early date. The reason for this becomes quite apparent when one takes into account the fact that the previously existing contract between the steelworkers union and the steel industry expired on New Year's Eve, 1951, with negotiations hanging fire for a number of months after that time. With 10 percent of employed soft coal miners working in the captive coal mines of the steel companies and nearly 20 percent of the nation's total coal

output being used by the steel industry, it would have been the height of folly for Lewis to have pulled his miners out at a time when the steel mills might be shut down anyway because of a steel strike.

However, when it was apparent that the steel strike was about to be settled, Lewis gave the required 60 days' notice to the northern coal operators of the termination of the existing wage agreement. The termination notice was written on July 22, only four days before the 54-day steel strike was settled on July 26. This was good timing, not only because the steel strike was about over but also because Benjamin F. Fairless, president of the U.S. Steel Corporation, had publicly expressed himself as being strongly against any further interruption in steel production. Such was also the attitude of the other major steel concerns which had just gone through the most costly strike in the history of the industry.<sup>5</sup>

Furthermore, the steel producers, with their ownership of captive coal mines, exercised a substantial, if not a major, voice in the policy determinations of the newly-formed Bituminous Coal Operators Association. It was only natural, therefore, that Lewis should press hardest to secure a quick agreement with this group, knowing that once he was able to sign up any substantial segment of the coal operators, such as was represented by this coal operators' association, the other operators would have to fall in line quickly or find themselves faced with a loss of markets which might prove to be permanent.

<sup>5</sup> *New York Times*, July 29, 1952.

The actual wage negotiations, like those which led to the surprise 1951 agreement, took place in utter secrecy and involved only three persons—Lewis, head of the miners; Moses, head of the northern Appalachian operators; and Moody, head of the southern operators. This type of person-to-person negotiation was in great contrast to the typical coal negotiations of the past where great numbers of miner representatives met with great numbers of operator representatives in the Central Competitive Field Conferences, the Appalachian Conferences, and finally the National Coal Conferences. It is true, of course, that these large negotiating committees on each side usually had to be “subbed” down into small groups of two or three from each side before the final job of reaching a new wage agreement was accomplished. But before that step had been reached a great deal of oratory had been channeled into the newspapers and a great many impossible demands, and charges and countercharges had been made on both sides. This new type of streamlined coal conference by-passed modern publicity techniques and seemed to reach quicker, if not better, agreements than its predecessors.

Although Lewis seemed to spend most of his time with Moses, head of the northern operators, he did not neglect the southern operators after he gave them the 60-day notice of contract termination on August 1. It was to Moody, rather than to Moses, that he proposed his new scheme of penalty payments for all days worked over three a week. This new share-the-work-plan was expected to have special appeal to

the southern operators, many of whom had been working their mines only three or four days a week. Lewis's three-day-a-week plan was rejected by the operators in 1949 and the northern operators have no more taste for it now, particularly the operators of captive mines which are working five or six days a week. If such a penalty program were adopted, it would mean that the steel companies would have to curtail their own mining operations and go into the commercial coal market to purchase the balance of their coal requirements.<sup>6</sup> This was exactly what Lewis had in mind (in order to share the available employment among his miners), and he thought such a scheme might be very attractive to southern operators and operators in the outlying fields who were running at less than full capacity.

It was this old tactic of successfully playing off one group of operators against another that once again brought Lewis a juicy contract for his miners when he got the northern group of operators to agree to his terms on September 20. Most mineowners in the outlying fields (i.e., those in Indiana and Illinois and those west of the Mississippi) had already indicated that they would accept whatever contract was signed by the Bituminous Coal Operators Association.

In addition to playing one group of operators off against another, Lewis used another time-tested tactic in his bargaining with the operators. Mindful of the record-high stockpile of coal, he invoked his power of calling memorial periods under the coal contract to in-

<sup>6</sup> *Ibid.*, August 26, 1952.



form the miners, the operators, and everyone else concerned that no coal would be mined for a 10-day period to begin on Saturday, August 23, with resumption of production on Tuesday, September 2. It was estimated that at least nine million tons of coal production would be lost as a result of this shutdown.<sup>7</sup> Although a safety inspection cleanup may have been one motive for calling this work stoppage, certainly another one was that of providing economic pressure on the coal wage talks. The loss of nine million tons of possible coal production had the effect of reducing by more than 10 percent the 80-million-ton stock of coal above ground. To the extent to which this reduction of the stockpile helped firm coal prices, the operators as well as the union benefited from this stoppage.

### Pressures on the Union to Settle

Although a certain group of the operators (the captive-mine operators) were under strong pressures to reach an agreement as quickly as possible, the union was also under strong pressures to avoid a strike this year. The pressures on the union may be summarized as follows: (1) the large coal stocks in the hands of the consumers, (2) the prevailing softness in coal prices with most coal selling below ceiling prices, partially because of a decline in export markets but mostly because of the inroads of competitive fuels,<sup>8</sup> (3) the threat from nonunion mines, which were producing 18 percent of total soft coal output, (4) the threat of wage

controls through the Wage Stabilization Board's possibly outlawing any settlement which was too far out of line with the prevailing wage agreements in American industry, and (5) the virtual certainty that the Welfare Fund would have to cease operations in the event of a strike.

(1) and (2) may be considered as being deterrents to the union's desire and ability to strike in the sense that any time the coal market is weak the speed and power with which union pressure can be brought to bear on the operators is greatly lessened. If coal stockpiles are very large the operators themselves are desirous of lessening this overhang of the coal market. Furthermore, the presence of an 80-day supply of coal in 1952 means that industrial consumers can simply continue operations at their usual rates a number of weeks after the onset of a strike. Therefore, the union threat to strike is less of a bogey for the operators when coal inventories are high and market prices are weak.

Of all these pressures, perhaps the most important was the certainty that the Welfare Fund would have to cease its payments if the mines closed down in a prolonged strike. The Fund depended for its existence on royalty payments of 30 cents a ton (40 cents under the new contract) for every ton of union coal mined. As it was, the Fund's receipts were barely matching its expenditures.<sup>9</sup> Thousands of miners and their dependents were receiving one or more types of benefit from the Fund.

<sup>7</sup> *Ibid.*, August 17, 1952.

<sup>8</sup> *Ibid.*, August 24, 1952.

<sup>9</sup> United Mine Workers of America Welfare and Retirement Fund, *Report for the Year Ending June 30, 1952*, p. 23.

Any interruption of payments to these beneficiaries touched a sensitive political chord in the United Mine Workers. The Fund had to cease all operations throughout the long months of strike in 1949-50. Even in June, 1952, it was in sufficiently serious financial difficulties that it had had to terminate free dental service to miners and members of their families.<sup>10</sup>

Not only were the miners extremely desirous of continuing the benefits available under the Fund; there were also many voices clamoring for an extension of these benefits. The outcry reached a sufficiently loud volume that Lewis himself had been forced to refer to this problem in his speech to the assembled United Mine Worker delegates in their October, 1952, convention in Cincinnati, Ohio. Lewis promised that higher royalty payments might be expected as the result of future wage negotiations so as to provide for these additional desired benefits.<sup>11</sup> Even a labor leader as strongly entrenched as Lewis must pay heed to political currents within his own organization. And there was no denying that the benefits provided by the Fund have been popular with the miners.

### The Quick Settlement

Perhaps the most astounding feature about the 1952 coal negotiations was the speed with which agreement was reached between the miners and the operators. The time of the actual bargaining was less than 60 days, which is something of a record (the 1951 negotiations excepted) for the attainment

of an industry-wide contract calling for record high wages and increased royalty payments to the Union's Welfare Fund. The previous section indicated some of the pressures acting on the union for a quick settlement. In fact, if the truth were stated bluntly, the mine workers' union was in a relatively weak bargaining position this year from various points of view. Yet the operators gave in with what seemed to be almost indecent haste. Why?

For one thing, the captive-mine operators had every reason to desire a quick settlement rather than a strike. The steel companies had just gone through the most costly strike in their entire history with the steel workers being out for 54 days. During the summer and fall of 1952 steel was in great demand and there were healthy profits to be made if the steel firms could operate at full capacity. Sooner or later a prolonged coal strike would cause the banking of the steel furnaces in a slow strangulation of the steel industry. Furthermore, the cost of coal has always been a small proportion of the total cost of steel so that an increase in miners' wages does not raise the cost of steel very much. With steel in great demand, the steelmakers could well afford a small increase in their costs of production.

Although total captive coal production in 1950 accounted for less than 17 percent of total coal production in the United States, the steel industry produced nearly 66 percent of this captive production.<sup>12</sup> However, if purchases by

<sup>10</sup> *New York Times*, June 2, 1952.

<sup>11</sup> *Ibid.*, October 9, 1952.

<sup>12</sup> Computed from data in Bituminous Coal Institute, *1951 Bituminous Coal Annual*, pp. 15 and 68.

the steel industry are added to its own production of coal, the consumption of the steel industry in 1950 is seen to be nearly 20 percent of total coal consumption.<sup>13</sup> The important influence of the steel firms on the course of coal negotiations is not completely revealed in the above figures. Their leverage effect is even greater as a result of the formation of the Bituminous Coal Operators Association in 1950. Installed as president of this new group and armed with the responsibility of negotiating with Lewis was Harry Moses, former president of H. C. Frick Company, the captive-mine subsidiary of U.S. Steel. It was rumored that not all of the large northern commercial operators were happy over the terms of the contract negotiated by Moses with Lewis. A correspondent reported on October 3rd that "George Love, president of Pittsburgh Consolidated, biggest commercial coal company in the nation, held out for several days against the proposed contract, but finally capitulated when Moses argued that he was 'committed' to the 'one-ninety and ten' contract. However, Love was so furious at Moses that he threatened to demand a new bargaining setup in the future, whereby the captive and commercial coal companies would deal separately with Lewis."<sup>14</sup>

The southern coal producers, likewise, were not at all happy about the contract which the Bituminous Coal Operators signed with Lewis for the miners' union. Joseph E. Moody, president of the Southern Coal Producers'

Association, indicated that some member-owners would have to close down some of their high-cost mines even if the government raised coal price ceilings.<sup>15</sup> Several days later, in testifying before the Wage Stabilization Board, Moody indicated that he had been instructed by his board of directors to ask for approval of the signed contract although he, Moody, was against it. The possibility cannot be ruled out that the southern operators and some of the northern commercial operators signed the new coal contract in haste hoping that they would be able to bring pressure on the Wage Stabilization Board to disapprove at least part of the higher miner wages called for in the new contract. (This kind of phenomenon was not unknown in World War II. During this period of wage and price controls, businessmen would sometimes agree to higher wages with a union and then covertly ask the responsible government agency to disapprove of the negotiated higher wages.)

### Provisions of the Coal Settlement

The basic terms of the proposed new contract in soft coal were announced by Lewis and Moses on September 20, 1952, only one day before the strike deadline. The Southern Coal Operators, headed by Moody, fell into line several days thereafter so that the wage agreement for the entire industry was signed on September 29 and was to take effect on October 1, 1952, after the signing of the new contract.

However, Moses was quite careful in advising his association members that

<sup>13</sup> *Ibid.*, p. 129.

<sup>14</sup> Drew Pearson column, *Daily Illini*, [Urbana, Illinois], October 3, 1952.

<sup>15</sup> *Champaign-Urbana Courier*, October 1, 1952.



approval of the Wage Stabilization Board was necessary before the new contract could go into effect. He wrote his members that if the Board had not acted, or had acted adversely, by October 15, when checks containing the higher pay would normally be due, he would inform the union that "we cannot legally pay the increases until the approval is forthcoming."<sup>16</sup> This approval, as we have seen, was not forthcoming insofar as the total wage increase was concerned.

The three major provisions of the contract called for a wage increase, a royalty increase, and the formal institution of seniority in the coal fields for the first time. Minor contract changes related to the provision for safety consultations, the calling of memorial periods by the miners, and the inclusion of a no-escape clause for the operators to prevent them from seeking to evade the terms of the contract.

Wages were increased by a flat \$1.90 a day for all mine workers. The relevant wage section of the contract now read: "All mine workers, whether employed by the month, day, or tonnage, yardage, deadwork or footage rate, shall receive Eight Dollars and Twenty-five cents (\$8.25) per day in addition to that provided for in the contract which expired March 31, 1946."<sup>17</sup> This sentence in the contract clearly indicates the amount of postwar wage increases Lewis has been able to secure for his miners. Aside from the absolute amount of the increase, the significant thing to note is that "all

mine workers" received the same flat increase. This method of wage increases has the effect of lowering the percentage differentials previously existing between the various classes of skilled workers. This is the philosophy of egalitarianism in practice.

The tonnage payments to be made by the signatory operators to the United Mine Workers of America Welfare and Retirement Fund were increased from 30 cents to 40 cents for each ton of coal mined. The clause fixing the portion of total moneys to be used to provide for pensions or annuities for the beneficiaries of the Fund was changed so that the guiding rule was no longer to be "proper actuarial computations" but rather "the Trust's statistical experience." Furthermore, the Trustee designated by the United Mine Workers (Lewis) was not only to be the chairman of the trustees of the Fund but was also to be "the Chief Executive Officer." The administration of the Fund was to be more firmly under the domination of the United Mine Workers than ever before.

Formal recognition was finally taken of the secular decline of employment in soft coal mining which has reduced the total of employed miners from the peak figure of 700,000 in 1923 to less than 400,000 in 1952. The 1952 coal contract states: "1. Seniority in principle and practice shall be recognized in the industry. 2. In all cases where the working force is to be reduced, employees in each job classification at a mine with the least service, shall be laid off first."<sup>18</sup> This is the first time that any such provision has ever ap-

<sup>16</sup> *New York Times*, September 30, 1952.

<sup>17</sup> *National Bituminous Coal Wage Agreement of 1950, as Amended September 29th, 1952*, p. 3.

<sup>18</sup> *Ibid.*, pp. 3-4.

peared in any industry-wide soft coal contract. The rising crescendo of demands from the rank and file to inaugurate some such system of seniority formally was finally taken into account by Lewis in his demands on the operators. (Clear indication of the increase in such rank-and-file sentiment can be found in the resolutions presented by the various local unions to the national conventions of the United Mine Workers in recent years.)

One of the minor changes found in the new contract provides that representatives of the United Mine Workers and representatives of the signatory operators shall hold joint consultations with the Bureau of Mines in order to revise the Federal mine safety code. Any revised code adopted by the contracting parties is to be made a formal part of this 1952 agreement. Another small change was included under the mine safety provision of the contract in that the United Mine Workers were now permitted to designate memorial periods not exceeding a total of 10 days in place of the previous five. (Lewis had actually called a 10-day memorial period in August under the old contract but he was able to do it because only five working days were involved.)

In order to prevent the possibility of any of the signatory operators attempting to evade or escape the provisions of the wage agreement, a clause was inserted making it explicit that this agreement applied to all of the coal lands owned or held under lease by the signatory operators. And, furthermore, "the said Operators agree that they will not lease out any coal lands as a

subterfuge for the purpose of avoiding the application of this Agreement."

### The Role of the Government

Historically, the Federal government has had an important role to play in crucial coal negotiations. The government has intervened as a mediator, an arbitrator, and a "fact-finder." It has secured injunctions against the union and has been able to persuade the courts to levy heavy fines on the union when some provision of the injunction has been violated. The government has even seized the mines on occasion and concluded agreements with the union which the operators have later had to accept as a *fait accompli*.

The main difference between Federal intervention this year and that of previous years is that in 1952, for the first time, the government has stepped in to disallow the full amount of increased wages called for in the concluded contract. This unprecedented action was taken on a split decision of the Wage Stabilization Board. The six labor members of the Board voted for allowing the full wage increase, whereas the four public members of the Board (there are two public member vacancies) joined with the six industry members in voting that only \$1.50 of the proposed \$1.90 could be allowed under the existing rules of the stabilization program. What was behind this decision of the Board?

For one thing, the Board did not like the pressure tactics used by Lewis to try to get them to agree to the terms of the new coal contract. Refusing to appear before the WSB himself to defend the terms of the new contract,

Lewis called for a strike on October 18 if the contract was not operative by then. He declared at the United Mine Workers convention in Cincinnati, Ohio: "I don't want any union to go to work on the 18th unless it is found that the welfare is paid. There are no ifs, and buts about it. The morning of the 18th is the deadline."<sup>19</sup> Archibald Cox, chairman of the WSB, and the other public members of the Board did not relish this "guns at the head" approach.

The public members of the Board, as well as the industry members, felt that if the entire amount of the negotiated wage increase were allowed, what was left of a weak stabilization program would be completely wrecked. Although the 1952 round of wage increases had already been granted, this spectacular new contract was likely to induce other labor leaders to attempt to emulate the miners' head in their 1953 wage demands. Union leaders have been prone to take account of the amount of wage increases and other improved worker benefits achieved by their rivals in the trade union movement. And Lewis has always been a stormy petrel to watch. Other union leaders would be forced to take aggressive steps in 1953 negotiations so as not to lose status as compared with Lewis in the eyes of their members. With the possibility of further wage increases, prices would be very likely to rise (or at least pressure in that direction would be generated) and thus the stabilization program might well be blown sky-high.

Although the Board's decision had

the effect of reducing the negotiated wage increase from \$1.90 a day to \$1.50, the door was left open for a possible settlement between the operators and the miners whereby the 40 cents could be restored by increasing certain of the fringe benefits enjoyed by the miners.<sup>20</sup> The form this increase might take could be in higher vacation pay, higher paid holidays, higher night-shift differentials, or higher royalty payments. Precedent for possible approval of such higher fringe payments can be found in the September 26, 1952, ruling of the Wage Stabilization Board that royalty payments to the Health and Welfare Fund in the anthracite industry could be increased without prior WSB approval. Harry Weiss, executive director of the Board, stated in a letter to the UMWA, "You are advised that prior Board approval is not required before the affected employers may increase their contributions to the Anthracite Health and Welfare Fund from 30 cents a ton to 50 cents a ton, provided that such increase in contributions is necessary to maintain the level of benefits prevailing on January 25, 1951."<sup>21</sup> Contributions to the Bituminous Fund were increased only from 30 cents to 40 cents a ton so that this decision in the Anthracite case could have provided the basis for the Board's approving an additional 10-cent contribution to the Bituminous Fund. Approval of possible increases in some of the other fringe payments in coal could be based on the argument that such increases would bring some of

<sup>20</sup> *New York Times*, October 19, 1952.

<sup>21</sup> Wage Stabilization Board, press release dated September 29, 1952.

<sup>19</sup> *Champaign-Urbana Courier*, October 16, 1952.



these fringe benefits only up to levels comparable with those enjoyed by workers in other industries. (Shift differentials of three cents an hour for the second shift over the first and six cents an hour for the third shift over the first in the soft coal industry are exceeded in many other industries.<sup>22</sup>)

The unfavorable decision of the Wage Stabilization Board was very quickly appealed by the United Mine Workers and the Bituminous Coal Operators Association acting in concert. A joint petition of these two organizations was filed with Roger L. Putnam, head of the Economic Stabilization Agency, on October 24, less than a week after the all-out stoppage of coal production. In their petition the two parties made it clear that they felt the proposed increase of \$1.90 a day was well within the wage stabilization formula and that they regarded as unfair the action of the Wage Board in refusing to approve their agreement in its entirety.<sup>23</sup> It should be noted that the Southern Coal Producers Association was not a party to this petition.

The next move took place soon after the submission of this petition, with President Truman calling a special meeting at the White House. Invited to this conference were Lewis for the miners, Moses for the operators, Economic Stabilizer Roger Putnam, David Cole, director of the Federal Mediation and Conciliation Service, and John R. Steelman, special assistant to the President.<sup>24</sup> At this conference President Truman asked Lewis directly to call off

the coal strike. Presumably no explicit assurances of reward were given save that Lewis's demands would get a fair hearing. Immediately after this meeting Lewis sent a telegram to his district presidents which read in part: "It will require a reasonable time for review of attendant facts and the reaching of a decision. It is my opinion that our industry should be operating during that period and that the best interests of the mine workers and the public will thus be served."<sup>25</sup>

How did it happen that this face-to-face meeting between two men (Truman and Lewis) who have in the past had harsh things to say about each other in public resulted in this immediate order to the miners to return to work? The obvious answer is to be found in the political milieu. This coal strike occurring on the eve of the national election was embarrassing both to the Administration and to the mine leader. Not only were the Democrats anxious to retain political power, but Lewis was supporting the Democratic ticket this year. It would be ironic at best to have Lewis campaigning for the Democrats while his miners were striking against the Democratic Administration. As one Pennsylvania miner put it: "I don't think the union organization wants to hurt Stevenson with the election so near."<sup>26</sup>

President Truman announced on December 3, 1952, that he had decided to override the advice of all his Stabilization officials and grant the full amount of the wage increase called for in the

<sup>22</sup> *New York Times*, October 19, 1952.

<sup>23</sup> *Ibid.*, October 26, 1952.

<sup>24</sup> *Ibid.*, October 27, 1952.

<sup>25</sup> *Ibid.*, October 28, 1952.

<sup>26</sup> *Ibid.*



negotiated coal contract. He did this, he said, because he wished to forestall a coal strike with the subsequent national emergency which would likely develop in its wake in a few weeks. In his written directive, Truman declared: "Such an emergency would arise at just about the time my successor took office. I am not willing to take an action that will create a crisis for my successor."<sup>27</sup>

### Economic Implications of the Coal Settlement

After all of these weeks of delay, the government finally approved all of the terms of the coal contract as signed by the operators and miners on September 29. In that contract, as we have seen, wages are increased \$1.90 a day and operator contributions to the Health and Welfare Fund are increased 10 cents a ton.

It is clear, then, that the labor costs of mine operators have been increased appreciably. What effect will this have on the existing number of coal mines and coal companies? And what about the profitability of those companies still remaining in the industry? To answer the last question first, it is obvious that the over-all profitability of coal mining will tend to be reduced. The only way that coal companies can maintain their present levels of profits in the very near future is to increase their coal sales at the existing level of prices or else raise the level of coal prices. It is very likely that the coal industry will press for higher OPS price ceilings or possibly even the complete removal of ceilings over the price of coal. However, as was pointed out earlier, coal is currently

selling below its price ceiling. Furthermore, as was also mentioned earlier, the operators attempted to raise the price of coal after the 1951 hike in wages and found a few months later that as a result of sagging demand coal prices were lower than they had been before the wage increase.

In the light of the decline in coal production this year as compared with 1951, as shown in the accompanying chart, it appears very unlikely that coal operators will be able to increase the price of coal sufficiently to take account of the higher labor costs imposed upon them by the new contract. Furthermore, in terms of the immediate past history of the industry vis-à-vis competitive fuels, it seems unlikely that coal companies can increase their sales at the present level of prices. If this is so, it automatically follows that profitability will be reduced.

With profit margins being squeezed by the new coal contract, it appears that at least some of the marginal coal operators will be forced to discontinue operations. These marginal operators — those who are barely meeting their costs of production with their receipts now — are typically the smaller operators in the area of deep coal mining. Although any one of them may not employ much more than 400 miners (many of them employ fewer than this number), the total number of marginal mines forced to cease operations will probably be high enough to result in a measurable decrease in employment opportunities for coal miners.

Mechanization is a possible long-run technique for maintaining profitability in the face of initially higher labor

<sup>27</sup> *Ibid.*, December 4, 1952.

costs. Machines, however, are expensive and are becoming even more so. As a result of the expense involved, only the larger companies have enough capital to undertake widespread mechanization. One of the quickest ways of increasing the size of coal companies is through consolidation. Hence, these higher labor costs may encourage, to some extent, further consolidation of coal companies so as to secure the capital necessary for extending the amount and kind of mechanization.

Another possible result of this coal settlement is an increase in the percentage of total coal mined by strip mining. This sector of the coal industry has been expanding steadily over recent years in percentage terms<sup>28</sup> and a further boost will be given to this trend by the recent settlement. Labor productivity in the surface mines, as measured in tons per man-hour for all employees except office workers, is more than twice that in the underground mines.<sup>29</sup> Hence, an increase in labor costs encourages a shift of capital into that sector of the coal industry (strip mining) where labor costs are at their lowest relative level. This, again, means a decrease in employment opportunities since fewer workers are needed for every million tons produced in strip mining than are needed in underground production.

The insertion of the seniority clause in the 1952 contract, for the first time, means that the union has been forced to recognize the long-run decline in

employment opportunities for its members. Whereas 704,793 miners were employed in 1923, only 415,582 were listed as being employed in 1950.<sup>30</sup> And that trend which has persisted over recent years is almost sure to be continued by the wage provisions of the present contract. To take account of that fact, the union has been forced by internal political pressures to secure the seniority clause protecting its older members. The burden of decreased employment will, in consequence, fall on those with less service in the mines.

Domestic consumers may not be forced to bear any further costs in the form of higher market prices deriving from the higher labor costs of the coal industry if the assumption of a weak market for coal is correct. They may, however, incur additional costs if more of them decide to buy alternative heating equipment rather than continue to bear the uncertainty as to the continuity of coal supplies which is forced on them by periodic coal strikes. To the extent that domestic consumers are induced to switch to other fuels, miners will suffer a further adverse employment effect.

Many industrial consumers, on the other hand, are already equipped to burn either of two competing fuels (e.g., coal and fuel oil or coal and natural gas) and often consume whichever fuel is available in quantity and is cheapest in cents per million Btu. Most of these industrial consumers have adopted a postwar procedure of hedging against a coal strike by building up

<sup>28</sup> Bureau of Mines, *Bituminous Coal and Lignite in 1950*, p. 17.

<sup>29</sup> Bituminous Coal Institute, *1951 Bituminous Coal Annual*, p. 158.

<sup>30</sup> Bureau of Mines, *Bituminous Coal and Lignite in 1950*, p. 17.

large stockpiles of coal. A good deal of the present large stockpile of coal can be explained by this desire of industrial consumers to assure continued supplies of coal throughout any short or moderate-length strike.

Finally, the level of wages and other labor costs in the 1952 contract suggests once again that the operators need a stronger, more effective bargaining organization than they now have. The public interest is more effectively served, in the judgment of the author, by a more even balance of power be-

tween labor and management than now exists in the soft coal industry. There are many possible ways of dealing with this problem. Of all of these possible solutions, the one which may allow the greatest latitude for free collective bargaining, with a minimization of the necessity of government intervention, would be that solution in which the operators would cooperate more effectively in a stronger bargaining organization vis-à-vis the miners' union.

# *Beauharnais v. Illinois*: Bulwark or Breach?\*

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WHEN the Federal Supreme Court upheld the Illinois Anti-Hate Law<sup>1</sup> it gave added meaning to Justice Holmes' famous statement that "hard cases make bad law." According to Holmes, "hard cases" are those involving conflict between two or more irreconcilable constitutional principles. Such cases make "bad law" because they require that restrictions be placed upon certain socially valued concepts in order to preserve others. In any given case it is always questionable whether a proper balance has been struck between the competing principles.

In *Beauharnais v. Illinois* the Supreme Court was confronted with a difficult case in every sense of the Holmesian dictum. It was asked to uphold the constitutionality of Sec. 224 of the Illinois Criminal Code, making it unlawful to publish or exhibit any lithograph,<sup>2</sup> moving picture, or drama which portrays depravity, criminality, or lack of virtue of citizens of any race, color, creed, or religion; which exposes

any race, color, creed, or religion to contempt or derision; or which produces breach of the peace or riots. Defendant urged that this code section violates the liberty of speech, press, and assembly guaranteed by the due process clause of the Fourteenth Amendment. Thus, the Court was asked to balance freedom of discussion against security of reputation, liberty of inquiry against freedom from group defamation. The reconciliation of these two competing interests is a delicate and thorny task under the best of conditions. It becomes a critical task when viewed against the rising tide of incursions both on liberty of speech and on integrity of group reputation.

## Nature of the Problem

Not since the days of A. Mitchell Palmer and his antiradical raids has freedom of thought and discussion been subject to such a sweeping and paralyzing invasion. On the Federal level, the Smith Act, the McCarran Act, the Hatch Act, the Taft-Hartley Act, and the President's loyalty review program have all been upheld by the Supreme Court against vigorous charges that they violate First Amendment rights. Simultaneously, a flood of state statutes and municipal ordinances has placed severe limitations on the right of public employees to speak freely and to join organizations of their choice. Many of these laws have been upheld in the

\* EDITOR'S NOTE: This article examines the conflict between the doctrine of free speech, on the one hand, and the rights, on the other, of minority groups to security of reputation. The problem treated, since it involves the place of such groups in society and the protections and opportunities afforded them, is of economic as well as of social and political significance.

<sup>1</sup> Ill. Rev. Stat., 1949, C. 38, Div. 1, Sec. 471.

<sup>2</sup> The Illinois courts have interpreted the term *lithograph* to include any printed matter.



state and Federal courts. Added to these statutory restrictions have been the inhibiting effects of Federal and state investigating committees; state, municipal, and university loyalty oath programs; and a widespread campaign in the press and in periodical literature against heterodoxy of speech and opinion. The combined effect of these repressive activities has convinced many thoughtful persons that there is an immediate and pressing need to halt the disintegration of our speech liberties and to return the First Amendment to its traditional position within the constitutional system.

On the other hand, an accelerating vilification campaign against the reputations of racial, religious, and political minorities raises serious questions about the desirability of unfettered and irresponsible speech activity. The Peekskill riots, the Cicero, Illinois, disturbance, and the recent murder of Florida NAACP leader Harry Moore are only the more spectacular results of this campaign. Operating under the constitutional protection afforded by the First Amendment, a number of organizations have aimed sustained attacks at negroes, Jews, Catholics, and left-wing minorities. Such attacks are symptomatic of a wave of fear and hostility unprecedented in American history. They are indicative of a growing disdain for individual rights and democratic processes. Ultimately, they suggest the need to re-explore those elements of the constitutional system which are now unfortunately furnishing protection for speech activities not infrequently reaching the proportions of group defamation.

Thus, the issue presented in *Beauharnais v. Illinois* impaled the Supreme Court on the horns of a dilemma. A decision to uphold the Illinois law places yet a further restrictive interpretation on an already emasculated First Amendment. A decision favoring Beauharnais and his White Circle League provides legal license for the growing campaign of minority group vilification. That a majority of the Court chose the first alternative and held the Anti-Hate Law constitutionally applicable to Beauharnais is of little comfort and less help to social scientists. Speaking for a majority of the Court, Justice Frankfurter adroitly avoided most of the serious and deep-reaching issues presented by the case. A close analysis of his opinion will show that the vexing problem of group defamation is no closer to solution than it ever was, that no adequate standard has yet been provided for mediating between the conflicting demands of free discussion and clean reputation.

### **The *Beauharnais* Decision**

The facts in the case are few and simple. Beauharnais, as president of the White Circle League, caused to be printed and circulated in downtown Chicago a leaflet and a petition calling on the city government "to halt the further encroachment, harassment and invasion of white people, their property, neighborhoods and persons, by the negro . . ."<sup>3</sup> The leaflet asserted that "if persuasion and the need to prevent the white race from becoming mongrelized by the negro will not unite us,

<sup>3</sup> 343 U.S. at 252.

then the aggressions . . . rapes, robberies, knives, guns, and mariju ana of the negro surely will."<sup>4</sup>

Beauharnais did not contest the facts of the controversy. He admitted to composing and printing the pamphlets, to passing out bundles of them for distribution, and to organizing and directing the ultimate distributors. He alleged, however, that conviction could only be justified by a finding that the leaflets were "likely to produce a clear and present danger of a serious substantive evil that rises far above public inconvenience, annoyance, or unrest."<sup>5</sup>

In upholding the trial court, Justice Frankfurter characterized the Illinois Code Section<sup>6</sup> as an ordinary criminal libel law. Every American jurisdiction, he pointed out, provides for the criminal punishment of libels directed at *individuals*, a practice which has never been thought to violate the constitutional protection of the First Amendment. The single question raised by this case, then, was whether a criminal libel law designed to protect *collectivities* or *groups* has the same constitutional status as one aimed at protecting *individuals*. Frankfurter grounded his affirmative answer to this query on two arguments. First, the law of individual criminal libel is based on the tendency of defamatory utterances to cause unrest, disturbance, and breach of the peace. But defamatory statements di-

rected at large groups, such as racial minorities, are even more likely to occasion public disturbances. Thus, individual and group libel laws are justified by the same principle. Second, sufficient evidence exists to provide the Illinois legislature with a *reasonable basis* for concluding that the consequences of racial defamation in Illinois are frequently very serious.<sup>7</sup> "This being so, it would be out of bounds for the judiciary to deny the legislature a choice of policy, provided it is not unrelated to the problem and not forbidden by some explicit limitation on the State's power."<sup>8</sup> Frankfurter concluded that the First Amendment cannot be viewed as an explicit limitation on the State's power to enforce group libel laws. "Libelous utterances, not being within the area of constitutionally protected speech, it is unnecessary . . . to consider the issues behind the phrase 'clear and present danger'. Certainly no one would contend that obscene speech, for example, may be punished only upon a showing of such circumstances. Libel, as we have seen, is in the same class."<sup>9</sup>

Justice Frankfurter rests his opinion squarely on the alleged similarity of individual and group libel laws. Like obscene language, defamation of individuals represents a type of speech activity which traditionally has been placed outside First Amendment protections. Because *group defamation* involves the same evils as *individual defamation*, it, too, must be placed outside the Amendment's orbit. Frank-

<sup>4</sup> *Ibid.*

<sup>5</sup> 343 U.S. at 253. The trial judge refused to charge the jury with the necessity of finding the clear and present danger of a substantial evil in these leaflets. Instead, the jury was instructed to find Beauharnais guilty if it found that, in fact, he did publish and distribute the leaflets in a public place.

<sup>6</sup> *Supra*, p. 59.

<sup>7</sup> 343 U.S. at 259.

<sup>8</sup> 343 U.S. at 262.

<sup>9</sup> 343 U.S. at 266.

further therefore concludes that traditional speech tests — such as 'clear and present danger' — are not applicable to cases involving group libel.

### Evaluation of the Opinion

The difficulty here does not lie in the assertion that individual and group vilification are similarly situated with respect to the First Amendment. Although many state courts have attempted to develop a basic distinction between individual and group defamation in the area of criminal libel law,<sup>10</sup> it is suggested in the following analysis that such a distinction is invalid and that Frankfurter is correct on this point. However, neither Frankfurter nor the state courts have given sufficient attention to the initial assumption that libel of *individuals* is a type of speech activity which must remain outside First Amendment protections. If this assumption is incorrect, the free speech problems arising from group defamation situations cannot be easily dismissed. This basic assumption, then, requires closer inspection.

The notion that libelous attacks on individuals may not be included within that class of speech activities protected by the First Amendment stems from a basic confusion about the nature of defamatory language and the sanctions which are available for its control. Two categories of defamation have been established within the American legal system — civil libel and criminal libel. The former is designed to provide compensation to persons whose individual reputations are injured by libelous utterances. The latter is aimed at pre-

venting public disturbances which result from the indignation generated by defamatory attacks on persons or groups. While the relationship between civil libel and the First Amendment has emerged from the judicial process with relative clarity, the relationship between criminal libel and the First Amendment has tended to remain obscure. Within the free enterprise framework of American society the civil law of libel has answered a felt need to protect the economic position of individuals whose material success so frequently depends upon a clean reputation. The First Amendment, in contrast, might be viewed as a protection for those speech activities involving *public* policies and solutions to *public* problems.<sup>11</sup> Historically, the Amendment was added to the Constitution as an additional guarantee that criticism of government and its policies could be made with impunity. Throughout most of our judicial history, construction of the Amendment has rested primarily on the notion that freedom of discussion is the *sine qua non* of democratic government. The Amendment has functioned primarily as a guarantor of that free speech so indispensable to the process of self-government. The question to be resolved, then, is not whether recovery of private damages for defamatory utterances is inconsistent with the speech protection afforded by the First Amendment; rather, *civil* libel and slander may be viewed as lying completely outside this Amendment's orbit.

<sup>11</sup> See Alexander Meiklejohn, *Free Speech and Its Relation to Self-Government* (New York: Harper and Brothers, 1948).

<sup>10</sup> *Infra*, pp. 63-64.

On the other hand, *criminal* libel laws are aimed at protecting the community rather than the individual. They are employed against those utterances which tend to disturb the good order of the state and to change the peaceful process of self-government into temporary anarchy. Malicious defamation of racial, religious, or political minorities is usually a speech activity designed to influence the public decision making process.<sup>12</sup> (Racial and religious groups, no less than political organizations, embrace political aims and engage in political action.) Therefore, the application of criminal penalties to libel situations collides head-on with the First Amendment, since constitutional guarantees of free speech are designed precisely to protect discussion of public issues.

Thus, Justice Frankfurter's assertion that individual defamation, and hence group defamation, are speech activities which cannot claim First Amendment protection results from an initial failure to distinguish clearly between the purposes of civil and criminal libel laws. He justifies the punishment of libelous attacks on racial groups by pointing to the tendency of such attacks to incite public disturbances; that is, he invokes the *criminal* law of libel. In doing so, he authorizes limitations on speech which is designed to influence the public decision making process, and which thereby falls within the first Amendment's orbit. This latter implication he

conveniently ignores, however, by the prestidigitatorial feat of placing criminal libel penalties in the same category with civil libel penalties, and thus removing both of them from the First Amendment's scope. Closer attention to both the theory of defamation and the theory of the First Amendment might have eliminated this difficulty.

Earlier decisions by state appellate courts avoid many of the undesirable consequences following from Justice Frankfurter's opinion. State courts have generally been unwilling to apply criminal libel punishments to the vilification of large racial and religious groups. The opinions of these courts rest on such doubtful logic, however, that they offer no solutions for Justice Frankfurter's difficulties. While criminal defamation laws exist in every state of the Union, they have never been employed with much success against those who vilify loosely knit social groups. Only small, well-defined collectivities such as fraternal organizations and labor unions have prevailed in libel litigation. In a series of cases involving defamatory attacks on the Knights of Columbus, the courts of three different states found against the defamers.<sup>13</sup> The New York Court of Appeals accurately summarized the prevailing judicial attitude toward group libel controversies: "The foundation of the theory on which libel is made a crime is that by provoking passions of persons libeled, it excites them to violence and breach of the peace. Therefore, a criminal prosecu-

<sup>12</sup> Beauharnais and his White Circle League employed defamatory attacks against the negro race as part of a campaign to influence public policy with respect to inter-racial housing.

<sup>13</sup> *People v. Turner*, 154 Pac. 34 (Calif. 1915), *Crane v. State*, 166 Pac. 1110 (Okla. 1917), *Alumbaugh v. State*, 147 S.E. 714 (Ga. 1929).



tion can be sustained where no civil action would lie."<sup>14</sup>

In actions involving unorganized groups such as races and religions, however, the courts have employed an entirely different line of reasoning. Convictions cannot be obtained unless particular members of the defamed group can demonstrate an injury to *personal* reputation. This is a proposition which usually cannot be established. In *People v. Edmondson*,<sup>15</sup> the Court of General Sessions of New York, after exhaustively reviewing the historical development of criminal libel law, asserted that "no indictment as one based on defamatory matter directed against a group or community so large as 'all persons of the Jewish religion' has ever been upheld in this or any other jurisdiction."<sup>16</sup> The court concluded that no member of the Jewish race could ever consider his personal reputation damaged simply because of a general written attack on the race. Therefore, no conviction for such a publication could ensue.

Thus decisions involving defamation of small, formal groups have been rested on a tendency-to-disorder argument, whereas those involving large, amorphous groups have been based on personal-injury grounds. The difficulty here is obvious. The only significant difference between these two lines of cases lies in the nature and size of the groups involved, yet this difference hardly affords a relevant criterion for distinguishing between the two tests. If vilification of small groups is criminally

punishable because it tends to incite disorder, then defamation of large groups should be equally punishable on the same grounds. Moreover, under certain conditions attacks on religious and racial minorities are even more likely to induce violence than are attacks on small organizations. No adequate judicial explanation has ever been presented for the failure to apply a tendency-to-disorder test to the defamation of racial, religious, or other social groups.

### The Dissenting Opinions

The problem of reconciling group libel penalties with the requirements of the First Amendment cannot be solved by drawing an artificial distinction between defamation of small groups and defamation of large groups. If restrictions on the former are justified, then restrictions on the latter are equally justified. Whether the object of the defamatory attack is an individual, a small, well-defined group, or a large collectivity, the gravamen of the offense will be the same. Moreover, legislative and judicial limitations on such defamatory utterances raise the same constitutional problems with respect to the First Amendment, regardless of the size of the group under attack. Justice Frankfurter recognized and accepted these propositions in his *Beauharnais* opinion. However, neither he nor the state appellate courts attempted to explore the relationship between criminal libel as a general concept and the requirements of the First Amendment.

Thus, Frankfurter's opinion in *Beauharnais v. Illinois* avoids the inconsistency of earlier state decisions by

<sup>14</sup> *People v. Eastman*, 81 N.E. 459 (1907).

<sup>15</sup> 4 NYS (2nd) 257 (1938).

<sup>16</sup> 4 NYS (2nd) at 259.

extending criminal libel protections to large collectivities. Symmetry is achieved, however, at the expense of the First Amendment. If legislatures are to be left free to "experiment" with solutions for social issues, if any solution which is "reasonably related" to the problem is constitutionally acceptable, then the First Amendment becomes a fiction.<sup>17</sup> As we have seen, Frankfurter's assertion that defamatory utterances lie outside First Amendment protections is untenable. That assertion rests on the invalid premise that *civil* libel and *criminal* libel laws stand in a similar relationship to the First Amendment. The implications of Frankfurter's position for freedom of speech cannot be eliminated merely by ignoring them.

If the majority opinion places serious limitations on freedom of expression, the dissenting opinions of Justices Black, Reed, Douglas, and Jackson produce equally serious consequences, both for minority group reputations and for self-government generally. The four dissenters invoke the well-worn "clear and present danger" doctrine as the only legitimate interpretation of First Amendment freedoms. Speech may never be abridged unless it poses the clear and imminent danger that certain serious and substantial evils will follow forthwith. The dissenters conclude that the defamatory language employed by *Beauharnais* and his White Circle

League cannot be placed in this category. Moreover, they imply that the speech activities of group libelers seldom, if ever, present such a high degree of danger as to justify their suppression under this concept. They therefore conclude that the Illinois law was unconstitutionally applied to *Beauharnais*.

It is patent that if "clear and present danger" continues as the dominant interpretive canon of the First Amendment, vilification of minority groups must go unchecked. But it is equally clear that if restrictions on group defamation can only be achieved by giving legislatures carte blanche to punish any utterances which they believe to be dangerous, then the First Amendment is in grave danger of destruction. This dilemma can best be avoided by developing an interpretation of the First Amendment which realistically reflects contemporary social conditions. Neither Frankfurter's "inherent tendency" doctrine nor the "clear and present danger" concept has successfully coped with the flood of new speech situations inundating the courts in recent years. Particularly is this true of the group libel problem.

### Theories of the First Amendment

It must be assumed at the outset that freedom of speech and discussion are indispensable to the success of democratic institutions. The acceptability of any solution to a specific speech problem should depend ultimately on the validity of the theory of self-government to which that solution is anchored. The political theory behind Frankfurter's *Beauharnais* decision is easily seen and easily refuted. Essentially, it is the

<sup>17</sup> The doctrinal upshot of Frankfurter's opinion is to return the First Amendment to the status which it occupied in the early twenties. During this period, many vaguely-worded, dragnet laws aimed at Communists, anarchists, and syndicalists were given judicial approval. See *Gitlow v. New York*, 286 U.S. 652 (1925).

notion of judicial restraint: Legislative bodies must be allowed the widest possible latitude in interpreting the meaning of "guaranteed" civil rights. Judicial interference with legislative decisions is justifiable only when those decisions are clearly and obviously in violation of the Bill of Rights. The legislative act is presumptively valid. This concept — which approaches perilously close to unlimited majority rule — must be viewed with much skepticism, particularly where legislative intolerance appears to be on the increase. Our experience in the twenties with criminal syndicalist and anarchist legislation, as well as with the more recent rash of antisubversive laws, should afford adequate evidence for the poverty of a judicial restraint notion.

The theoretical basis of the "clear and present danger" doctrine might well be characterized by the phrase "intellectual laissez-faire." This theory views public discussion as a mechanism for the statement of individual and group opinions; competition between opposing interests within the "market place" of public opinion is its basic concept. It seems to be implied that this opinion market is controlled by a self-adjusting mechanism similar to Adam Smith's invisible hand as it operates in the economic market place. Although each individual is exclusively concerned with and argues solely in behalf of his own interest, the automatic operation of the free opinion market will guarantee the emergence of the wisest possible solutions to public problems. Under this theory, only the immediate threat of a catastrophe which would forever deprive one or more of the contestants of the speech

weapon (such as violent overthrow of the government) can justify prohibition of speech.

Unfortunately, this laissez-faire concept is subject to many of the same criticisms attending its application to the economic market place. First, it fails to account for the disequilibrium produced by monopolization of the channels of communication. Concentration of the ownership of newspapers, periodicals, radio, television, and motion pictures in a relatively few hands, all having a somewhat similar social outlook, means that certain points of view will perpetually have a much greater opportunity for general acceptance. Second, there is little foundation for the assumption that clashes between selfishly oriented opinions will not produce results harmful to the society in general. When such opinions descend to the level of minority group defamation, for example, countless instances of economic and social discrimination are the inevitable and measurable result.

Both of these theories, then, and the speech doctrines which have been built upon them, have proved ill-adapted to the solution of contemporary social issues. What is needed is a theory which will relate the First Amendment more directly to the process of self-government. To accomplish this task it might be well to borrow a page from recent interpretations of the equal protection clause of the Fourteenth Amendment.

### A New Speech Test

The major problem to be solved whenever government limits any activity or places restrictions on any type of action is one of classification. This

is equally true whenever government places limitations on speech activities. Two considerations are involved when such restrictions are imposed. First, the class of speech activities which is singled out for restriction or prohibition must bear a *reasonable relationship* to some public objective. Second, the public purpose to be effectuated must be a *valid* one. For example, when the city of Lockport, New York, places limitations on the use of sound trucks and other amplifying systems in public places, such special treatment of a given type of communication device must bear a reasonable relationship to some valid community objective. In Lockport's case, sound truck limitations were designed to reduce public annoyance and inconvenience.<sup>18</sup> But restrictions on this class of speech activities need not be designed to accomplish such a limited objective. In fact, in the Lockport case there is considerable doubt as to whether this narrow objective is a valid one when it is measured off against the disadvantages which follow from restricting the dissemination of ideas. Rather, in every case where speech activities are limited, the public purpose to be achieved should be thought of as the *maintenance and improvement of our capacity for self-government*. Speech restrictions should be tested only by determining whether they do or do not contribute to the process of self-government. If any other public objective is used as a basis upon which to classify and limit particular utterances, drastic and intolerable interferences with the communication of public ideas will most likely result.

<sup>18</sup> See *Saia v. New York*, 334 U.S. 558 (1947).

The question of reasonable relationship between classification and objective remains to be investigated. From the development of equal protection doctrine the notion has emerged that a reasonable relationship exists when the class singled out for special treatment incorporates all or most of that trait or characteristic which the community has found it necessary to suppress.<sup>19</sup> All persons standing in a similar relationship to the law's objective must be similarly treated. Further, there must be compelling reasons why the community's objective cannot be achieved without the imposition of certain restrictions on the particular class which has been singled out for special treatment.

Finally, attention must be given to the application of such a speech test to utterances of a defamatory character. Can it be asserted that defamation of racial, religious, and perhaps political minorities perverts the communication process to such a degree that it poses a real threat to the institutions of democratic government? Is there a reasonable relationship between restrictions on this class of speech and the maintenance of self-government? The answer to both of these questions can only be supplied by closer observation of the real character of intergroup hostility and group defamation.

Antagonism and hostility, opposition and disagreement among all types of groups and collectivities in a free society are probably inevitable and to a certain extent desirable. The use of

<sup>19</sup> See Joseph Tussman and Jacobus tenBroek, "The Equal Protection of the Laws," *California Law Review*, XXXVII (September, 1949) 341-381.



speech weapons for the implementation of oppositional attitudes would seem to be equally inevitable. There is a point, however, at which opposition and disagreement become intolerance and prejudice. It is suggested that certain antiminority prejudices are of such a nature as to reflect a basically antidemocratic or authoritarian personality structure on the part of those who accept and articulate them. In recent years the attention of many psychologists and psychiatrists has been increasingly focused on the nature of ethnocentric personality syndromes.<sup>20</sup> Most of these authorities seem to agree that racial prejudice is the most serious manifestation of ethnocentrism in contemporary American society. There is much less agreement as to the precise clinical nature of race prejudice. Two general conclusions, however, seem to have achieved a rather wide acceptance. First, such prejudice may be either a neurosis or a psychosis, depending upon the degree of intensity with which the attitudes are held.<sup>21</sup> Second, the presence of strongly prejudiced behavior patterns usually is indicative of an underlying personality

structure which is consistently rigid and inflexible. The exact nature of these personality rigidities still remains a matter of conjecture. However, the work of the California Associates on the Authoritarian Personality Studies suggests some significant characteristics of the prejudice syndrome.<sup>22</sup>

This survey showed that prejudiced persons have many deep-seated, unsatisfied needs. *Primary* among these is the frustrated need for affection and security. Such persons usually have not developed an adequate superego, or conscience, and thus they seek a strong authority source outside themselves. Such source usually is found in the form of membership in some in-group whose values can be accepted and implemented without first being scrutinized. *Second*, a need to protect the authority source with which identification has been made frequently leads to the tendency to reject, condemn, and punish people who violate conventional values. *Third*, prejudiced persons are likely adherents to the *Führerprinzip*: they are preoccupied with a dominance-submission, leader-follower pattern and they tend to glorify strength. They appear unable to conceptualize strength as inherent in patterns of cooperative behavior. That is, they fail to realize that true cooperation involves the free and spontaneous contributions of recognized equals. *Finally*, the need to justify their own unconscious internal destructive impulses leads them to project this destructiveness onto the outside world and to believe that wild

<sup>20</sup> Ethnocentrism may be defined as "general rejection of, and extreme hostility toward, certain specified social groups. It includes unquestioning acceptance of one's own in-group and complete rejection of all out-groups."

<sup>21</sup> The noted psychologist Ernst Simmel defines prejudice in the following manner: "Group prejudice is a clinical syndrome. It is unrestricted aggressive destructiveness under the spell of delusion, in complete denial of reality, and as such it is well known to us as a psychosis; it is a paranoic form of schizophrenia." Ernst Simmel, ed., *Anti-Semitism: A Social Disease* (New York: International Universities Press, 1946), p. 39.

<sup>22</sup> Theodore W. Adorno, et al., *The Authoritarian Personality* (New York: Harper and Brothers, 1950), 990 pp.

and dangerous conspiracies are being formed against them by one or more out-groups.

Although this brief list of the basic needs of prejudiced persons is far from exhaustive, and although much scientific investigation remains to be done before such a personality pattern can be ascribed to all or most ethnocentric individuals, it does provide strong grounds for believing that both the minority group libeler and his more receptive auditors are basically antagonistic to the democratic process. A preponderance of these needs, if reflected in the behavior patterns of members of groups found to be in violent disagreement with each other, would indicate the presence of a type of hostility considerably surpassing the more tolerable attitudes of opposition and contention inherent in all democratic societies. It is these ethnocentric attitudes which, if widespread, would render democratic functioning impossible.

This analysis, then, lends much support to the conclusion that a reasonable relationship does exist between restrictions on group defamation and the maintenance of self-government. To the extent that the more vigorous forms of minority group defamation are psychotic, or at best neurotic, phenomena, and to the extent that racial prejudice in particular and ethnocentrism in general are authoritarian attitudes, then to that extent do the activities of group libelers contribute to the disintegration of free society. The establishment of a reasonable relationship between limitations on ethnocentric utterances and the maintenance of self-government will require, in every case, a twofold inquiry

into the specific class of statements which the State proposes to restrict. First, the trait falling within the prohibited classification must be identified. The degree of ethnocentrism (prejudice) represented by the speaker's statements must be determined in as accurate a manner as possible. Second, the relationship between the trait so classified and the objective, maintenance of the democratic process, must be established. Thus, the degree and nature of the public's hostility toward the defamed group must be ascertained or recognized. If the degree in each case is found to be sufficient to indicate the presence of psychotic or neurotic hostility patterns representing a severe distortion of reality, then it may be concluded that a reasonable relationship between the classification and the objective has been established.

It is certain that many legitimate objections can be raised against the importation of such a free-speech test into our constitutional structure. It may be argued that there is at present insufficient evidence and understanding about the nature of psychological hostility patterns; that therefore it would be impossible for courts and legislatures to determine whether the requisite degree of pathological hostility existed in any given case. It may be further argued that neither courts nor legislatures are equipped to apply such precise psychological standards as those suggested here. While there is much truth in both these allegations, it must be remembered that no task involving legislative and judicial line-drawing is an easy one. Admittedly, the line between pathological hatred and abuse,

and the more tolerable degrees of enmity which will probably remain a constant factor in intergroup relations, is a difficult one to draw. It is doubtful, however, whether that line is any harder to locate than the one between speech which represents the clear and present danger of a substantive evil and speech which does not pose such a threat, a distinction on which the First Amendment rested for nearly two decades.

The development of a full-blown solution to the problems generated by group defamation is obviously beyond the scope of this brief paper. The major purpose here has been twofold: first, to indicate the great need for controlling a rising tide of intergroup prejudice in the United States without at the same time destroying First Amendment freedoms; and second, to suggest the general lines along which a solution might be developed. If the need is held to be sufficiently great, then the development of a precise test along the lines suggested here should not prove to be an unsurmountable task.

### Conclusion

In conclusion, it is suggested that the application of these equal protection concepts to the interpretation of the First Amendment would resolve the dilemma which trapped the United States Supreme Court in *Beauharnais v. Illinois*. The interpretive device offered here would eliminate the legislative license so gratuitously extended in Justice Frankfurter's opinion. Both legislatures and courts would be restricted in their speech-limiting activities to curbing those types of utterances

directly and intimately affecting the process of self-government. Further, this approach sidesteps the highly inflexible and rigid "clear and present danger" doctrine used in the dissenting opinions. It offers at least one method for adjusting the delicate balance between freedom of speech and security of reputation without completely sacrificing either one or the other. It cannot be overemphasized that the rights of free speech and good reputation are but two sides of the same coin, a coin with which democratic citizens purchase the advantages of self-government.

The well-intentioned person accepts freedom of speech as a well-established value in this society. Thinking people have lately come to realize that individual reputation is identified with group reputation. The individual today is effective in gaining his political ends only insofar as he is a member of a pressure group or a political party. He achieves economic objectives and material security primarily because of membership in a labor union or a trade association. His social status is in large measure determined by the service, fraternal, or religious organization to which he belongs. Insofar as any of these groups is weakened, the individual member is weakened. Insofar as any group becomes the object of an active and widespread prejudice, to that extent are its members blocked in the realization of their political, economic, and social goals. If it is true that the increasing complexity of industrial civilization renders the individual increasingly impotent, then it follows that group action will grow

ever more important as the guarantor of personal well-being. It is this development which lends emphasis to the need for some type of control over group defamation.

Justice Black concludes his dissenting opinion in *Beauharnais v. Illinois* with the following remark:

"If there be minority groups who hail this holding as their victory, they might consider the possible rele-

vancy of this ancient remark: 'Another such victory and I am undone.'"

This significant insight tells only half the story. One might well paraphrase it with the assertion that "Another such victory for *either* freedom of speech *or* security of group reputation at the expense of the *other*, and we are all undone."



# Union Practices and Policies — The Members' View

## A Preliminary Report

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It is becoming increasingly apparent today that unions are an integral and significant part of our society, playing an ever-expanding role in economic and political affairs. Many statements have been made with respect to the effects of unionism upon the American worker — statements by management representatives, union officials, politicians, and social scientists. But unlike conclusions drawn about the effect of modern management upon the worker, there are few empirical data upon which to base these assertions. Therefore, any field study of the effect of the American labor movement upon its membership should be of particular interest. This article is a report on some aspects of one of the few empirical studies of internal union structure and functioning that has been done.

The field work was done in the 21 local unions which belonged to a regional organization of a joint-board type. In this organization, most major policy decisions were discussed and voted on by a regional board of elected members representing the local unions. Decisions of the board were then put before the membership of the locals for ratification.

A highly detailed questionnaire was

utilized as the research tool, dealing primarily with five major union activities: collective bargaining, the handling of complaints against management, the work of business agents, meetings, and political action. The first question included an over-all appraisal of the union and a general evaluation of the five activity areas, plus evaluation items on union dues and on the company for which the union member worked. The rest of the opinion questions dealt in detail with the five major activities. With the exception of question one, each question had three parts: (a) what should be done, (b) what was seen as being done, and (c) the feeling about what was seen as being done. The last section of the questionnaire contained personal data items.<sup>1</sup>

This article is based on the preliminary

<sup>1</sup> The questionnaire was mailed to a local-by-local random sample of rank-and-file members and to all stewards and officers. Later, the questionnaire was orally administered to a smaller sample of the union membership to supplement and check mail responses. A regional average was computed from a random sample drawn from each local sample, the size of the random sample being determined by the proportion each local's membership contributed to the region total. Both regional averages and local response totals were converted into percentages for each question.

nary report given to the regional union involved. The initial report was limited to the regional averages and was entirely descriptive, i.e., no attempt was made at this point to analyze the relationships existing among locals, between the region and the locals, among opinion areas, among the breakdowns of questions, or between personal data and particular questions. Such analysis is in progress at the present time.

### How Members Felt, in General

From 54 percent to 85 percent of the rank-and-file members expressed favorable opinions about all general union functions, i.e., the over-all job the union was doing, collective bargaining, the handling of complaints, the job the business agents were doing, union meetings, political activity, and dues. Favorable opinions were also expressed regarding the companies for which the members worked. (See Chart 1.) In general, the views of stewards and officers followed the same pattern as the rank and file, although they were more favorable to the union. From 62 percent to 83 percent of the stewards and officers expressed favorable opinions in each of the general areas. (See Chart 2.)

In general, very little distinct dissatisfaction was noted in these general areas either among rank-and-file workers or among stewards and officers. Union members showed the greatest dissatisfaction with meetings and dues, whereas the stewards and officers were most dissatisfied with meetings and business agents. In each case about 25 percent expressed unfavorable opinions.

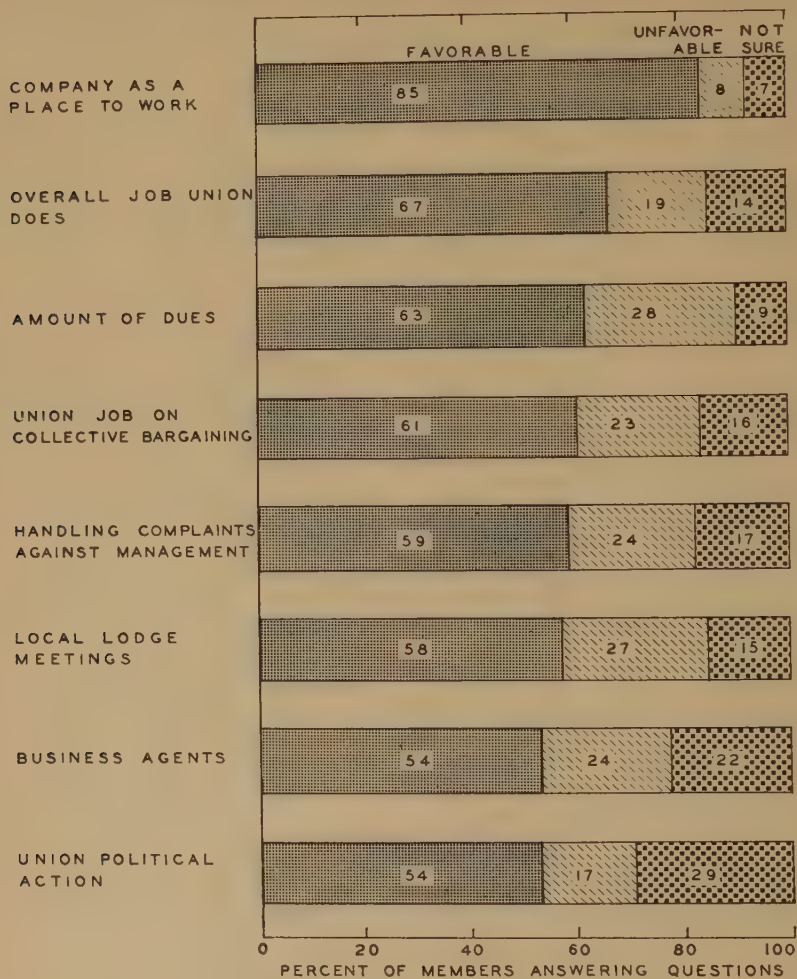
In all of the general evaluations of union activity, more members (9 percent to 30 percent) answered "undecided" than did stewards and officers (6 percent to 19 percent). (See Charts 1 and 2.) However, stewards and officers were slightly more "undecided" as to their feelings about the company in which they worked than were the rank and file.

### How Members Felt, in Detail

Examination of the detailed questions in the five major areas being studied made it possible to pinpoint dissatisfaction to some extent. In four of the areas, the point of greatest dissatisfaction was the same for stewards and officers as for members. The major criticism of collective bargaining methods concerned the amount of information the membership received about what was going on in negotiations. Most of the unfavorable responses with regard to business agents pertained to the part they played in running the regional organization. Adverse comment relating to meetings centered on lack of attendance. Disapproval of political action was focused on the part the union took in telling its membership whom to vote for. There was no outstanding objection among stewards and officers to the way complaints against management were handled, but members were dissatisfied with respect to information on what was happening to their complaints.

It was interesting to note that the greatest percentage of unfavorable opinions in the entire questionnaire both for stewards and officers and for

Chart 1. How Members Feel About the Union and Company in General



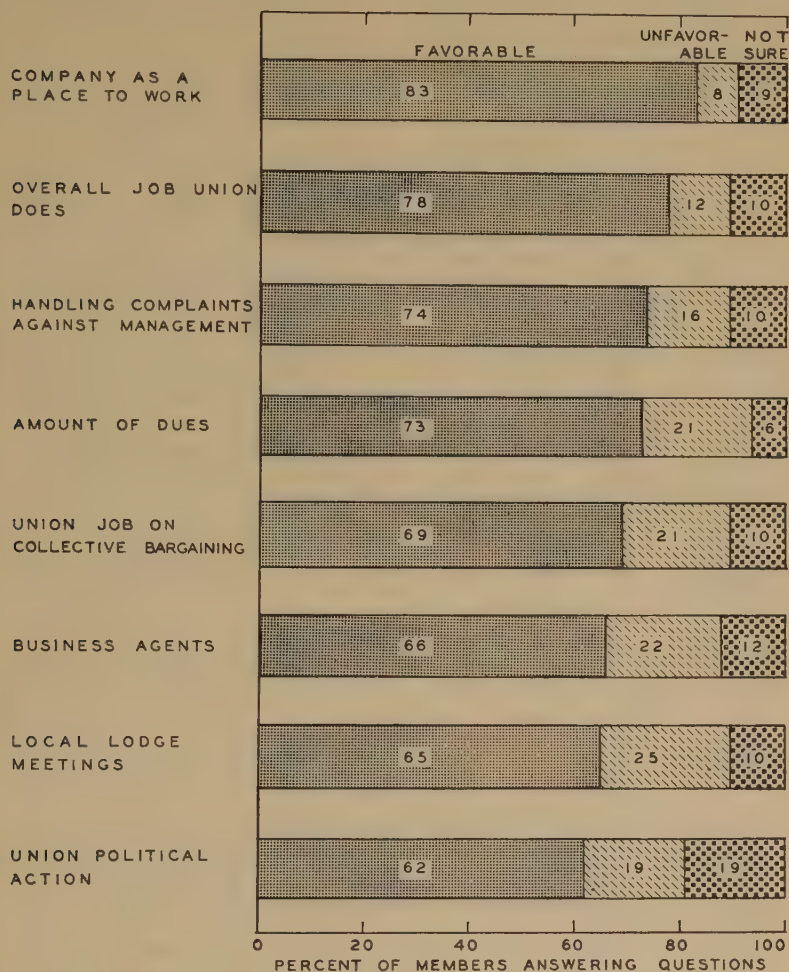
rank-and-file members centered on membership attendance at meetings, i.e., the membership seemed to be more dissatisfied with the behavior of their own group than with the behavior of their officials. This was the only area in which stewards and officers indicated even more dissatisfaction than the members.

### What Members Saw as Being Done

Up to this point, membership evaluation of the union has been discussed; but apart from the level of satisfaction, how did this group see their union as operating?

In each question at least 8 percent of the rank and file said that they did not know how the union operated, and in

Chart 2. How Stewards and Officers Feel About the Union and Company in General



some questions, the "don't know" answers ran as high as 31 percent. In general, they seemed to know least about what political action the union was taking. In this case the largest percentage of "don't know" responses concerned the extent to which members were asked for political donations.

The largest percentage of "don't knows" within each of the other four

major areas studied concerned the following points: the part the region took in setting collective bargaining policies for shop contracts; whether the union kept members informed as to what was being done on complaints; the extent to which the regional organization was run as its business agents thought best; and the extent to which shop meetings were held to discuss union problems.



Although stewards and officers followed the same pattern as the rank and file, a far smaller percentage of them stated that they did not know what was going on.

Among the members who indicated that they *did* know what was going on, there was considerable disagreement about what the union actually was doing. The extent to which members disagreed among themselves about how the union was operating was more pronounced in some areas than in others, although in no case was there consensus. The statements of what was going on were most consistent in the case of business agents, where the majority of the rank and file were in agreement concerning all phases of the business agents' activities that they were questioned about. There was also considerable consistency with regard to collective bargaining. However, while there was a good deal of agreement on specific phases of the remaining topics, this was not true for each subject as a whole. Except for politics and union meetings, stewards and officers were far more consistent among themselves about what the union was doing than rank-and-file members were.

### What Members Thought Should Be Done

Members were in substantial agreement on what *should* be done in all areas. This was also true of stewards and officers. Moreover, there was considerable accord between the two groups.

With reference to collective bargaining, it was interesting to find that there was least agreement on the extent to

which the union should emphasize wage increases, although even here 72 percent of the rank and file and 80 percent of the stewards and officers agreed that the union should "always or usually" emphasize increases.

The fact that there was considerable difference of opinion on the extent to which complaints should be settled as the members saw fit was of particular interest. This was the case for both rank-and-file members and stewards and officers, each group having a bare majority in favor of such policy being "always or usually" carried out.

Both stewards and officers and the rank and file were divided with regard to the part business agents should take in running the regional organization. Even in this case, however, about half of each group thought the region should "always or usually" be run as the business agents saw fit.

On these three topics — collective bargaining, complaints, and business agents — there was most agreement among the rank-and-file members on items concerning communications. More than 90 percent thought the union should "always or usually" keep them informed about what was going on in negotiations and about what was happening to their complaints. The same percentage also felt that business agents should "always or usually" explain anything the members wished to know about the union.

Eighty-five percent of the rank and file and 92 percent of the stewards and officers thought that members should "always or usually" attend their local meetings. This fact may seem somewhat paradoxical in the light of statements

of concern made by many union officials throughout the country over lack of attendance at union meetings. Apparently, the membership in this particular region shared the officials' point of view.

On the subject of the union in politics, more than 80 percent of both rank-and-file members and stewards and officers said that the union should support prolabor candidates. More than half of the members and two-thirds of the stewards and officers were of the opinion that the union should take an active part in politics.

One-third of the members, however, said that politics should "seldom or never" be discussed at union meetings. An even larger number, more than

half, said that they did not want to be asked for contributions for political action and that they did not want the union to tell them whom to vote for. In general, a slightly greater proportion of stewards and officers thought the union should play a greater role in politics.

### Summary

In summary, with the exception of political action, it appears that the membership was in considerable agreement as to what the policies and practices of their union should be. They did not, however, consistently see the union carrying out these practices and policies, nor were they unanimous in their degree of satisfaction.

## Books Reviewed

*The Economic System.* By E. T. Weiler  
(New York: Macmillan Company,  
1952, pp. xxx, 869. \$5.75)

This is a college textbook for the first course in economics — the “Principles of Economics” as it appears in college catalogues. As other authors have done in tackling this field, Professor Weiler has chosen to emphasize strongly the working of the economic system as a whole rather than the analysis of particular market structures or the problems of firms and households.

The volume consists of 38 chapters grouped into five parts. It is a highly integrated work, each chapter and each part leading into what follows, and there are strong common threads that run throughout: the point of view and the analytical method.

Part One, “The Economy and the Economizing Problem,” gives a preliminary view of the main structural features of a free market economy. The aggregative emphasis in the analysis is introduced here with suitable warnings as to the information which may be lost by such aggregation. The economizing problem is defined, the elementary units of the economy (at this stage only firms and households) presented, and some descriptive details of the structure of business firms recalled for the student. The simple circular flow aspect of an exchange economy is briefly outlined and the measures of this flow (quantities and prices) are set forth.

With these preliminaries out of the

way, Part Two, “The Mechanics of a Price Directed Economy,” sets up a simple static model of a competitive exchange economy and explains by this model how the price system affects and is affected by the choice decisions of consumers and firms in the products markets, and by the choice decisions of firms and resource owners (households) in the markets for productive services. It is in this section that the distinctive feature of this book, the continuing emphasis on the general flow diagrams of the whole economy, is first so clearly evident. The discussion is then intended to cover the effects of monopolistic behavior in some segments of the economy on the system as a whole. The analysis is directed mainly to the less-than-optimum allocation of resources that the private exercise of monopoly power is likely to bring about. The last chapters of this part are devoted to the expansion of the simple model to take account of the government and the banks, and to indicate how international trade (“the rest of the world”) fits into a model of a national economy. The flow diagrams here become more complicated, but each additional feature is introduced separately, then built into the preceding structure. The Fisherian equations are the main tools of analysis introduced, the Keynesian apparatus of a simple type being presented as a contrast in an appendix. This reviewer was particularly impressed with the simplicity and clarity with which a difficult job of exposition is handled in this section of the book.



Part Three, consisting of one long chapter and an appendix, gives a summary of the national income accounts of the United States for recent years and illustrates how these data may be fitted into the flow diagrams of the economy.

Part Four analyzes the flow of economic variables over time and outlines a conceptual framework that helps the understanding of the changing patterns of a dynamic economy.

In Part Five, Professor Weiler shifts from what he considers to be the areas of technical competence of an economist (the discussion of the problems concerned with the choice of means to given ends) to the broader and more ethical problems concerning the social choices of the ends themselves. It is here that he discusses such problems as the maintenance of a competitive economy, labor unions, farm policy, full employment, inequalities in personal incomes, social security, and international relations. To all these questions he brings a clear statement of the factual background and suggestive discussions and analyses as to the fruitful way to face up to the social questions involved.

The copyright notice indicates that this work has appeared in earlier forms. The lack of slips in wording or logic and the smooth and lucid exposition imply to this reviewer that this is a polished and repolished work, carefully pretested in the classroom and by student use.

The text seems to this reviewer to be aimed more at the student who is not likely to go further in economics; that is, emphasis is given to an over-all view

of the economy and to the application of the tools to problems of interest to the general citizen, rather than to the building of the foundations of partial equilibrium analysis and the study of market behavior and results. The result may be to create in the student an overoptimistic impression of his ability to achieve correct judgments or complete explanations on economic policy or of economic events. This may be inevitable with any approach, however, and many prefer this emphasis even for the courses designed as a foundation for later formal economics.

The flow-diagrams are so ever-present that some readers may forget that they are mere aids to exposition and come to think that the diagrams are the economy. This danger, that the tools are viewed as ends in themselves, is particularly a problem at the beginning level of work in economics.

Your reviewer cannot resist asking whether other readers have noticed zoological patterns in some of these flow diagrams, particularly Figure 8-1 (a wistful anteater?) and Figure 8-2 (a bashful giraffe?).

This volume exposes the reader to the important problems facing a free economy and treats them carefully and competently. This book might well be recommended to a broader business audience for those who wish to get a clear view of the economic structure of our society and a basic understanding of its over-all workings.

A workbook, keyed to this volume, is published as a companion volume. It consists of a wide range of questions on the materials of each chapter, mainly of the multiple-choice type,



with numerical problems when appropriate (as in the materials of the chapters in Part Two).

This is certainly one of the best of recent elementary texts and should please both the teacher and the student because of its straightforward approach and clear writing.

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*British Planning and Nationalization.*

By Ben W. Lewis (New York: Twentieth Century Fund, 1952, pp. xi, 313. \$3.00)

To many observers, the victory of the Labor Party in 1945 seemed to signal the beginning of a precedent-shattering period of policy experiment and innovation.

Looking back over six and a half years of Labor rule, Professor Lewis suggests that economic events in Britain, if they have entailed both experiment and innovation, have been anything but precedent-shattering. He also suggests that the results of Labor rule, while something less than is claimed by Labor's ardent protagonists, are something more than its impassioned adversaries would concede. Professor Lewis conveys these impressions not through argument, in which he indulges little, but through a reasonably detailed and suitably documented recitation of facts.

*British Planning and Nationalization* surveys major areas of policy development under the Labor Government's rule. More than a third of the book is given to an examination of the nationalized industries and the issues involved in nationalization. Four of the nation-

alization measures—involving the Bank of England, civil aviation, cable and wireless, and gas—are disposed of in a few pages. According to the author, they have aroused relatively little controversy and, to date, have involved little actual change. The coal, transport, electric power, and iron and steel industries are each treated more fully in separate chapters, as is the nationalized health service. Separate chapters also are given to town and country planning, the distribution of industry, housing, and agriculture, each of which loomed large in the Labor Government's program.

The book does not render, and makes no pretense of rendering, an account of all areas that have been affected significantly by recent legislation. For information on national insurance, various welfare services, antimonopoly policy, the development councils, and income redistribution, the reader must turn to other sources.

The volume begins, as well it might, with a useful and informative chapter on British economic planning. The various organizations with planning responsibilities, the methods whereby these organizations assay the country's needs and resources, the decisions how the two will be adjusted to each other, and the techniques to be used by the government in implementing the resultant plan are all considered in some detail. The whole procedure, says Professor Lewis, is less pretentious, detailed, and precise—and more limited in its influence on the economy's conduct—than is generally supposed. The government makes estimates, sets goals or targets for the principal economic

categories, and provides a framework through which it acts and within which actions occur. But the making of day-to-day decisions remains, as before, the task of individuals and individual firms. Uncertainties, mainly in the international field, make it impossible to prepare even a five-year plan that would serve as a useful guide. Lewis adds:

"The program does not purport to be inspired. It is hesitant and tentative; its goals melt easily into predictions and its predictions into hopes . . . but the nature of [the government's] intent cannot fairly be questioned. It is attempting to combine a free democracy and a planned economy, and where operating experience demonstrates that elements of the two are mutually exclusive, planning is subordinated to freedom."

Just how much such planning contributes or is capable of contributing to the positive direction of the economy remains, says the author, "an open question."

Succeeding chapters on the nationalized industries, and to a lesser degree the other chapters as well, follow roughly a single pattern. The problem background and legislative history are touched upon, the legislation enacted by the Labor Government is discussed, and the results of the changes are examined. Whether the outcome has, on the whole, proved favorable or gives prospect of developing favorably must be judged by the reader for himself. Stressing that the record covers too brief a period to allow definitive evaluation, the author proffers few strong conclusions. Not infrequently he juxtaposes

the views of the critics with those of the advocates, but here his role is that of referee rather than judge. On the whole he confines himself to a recitation of the issues — new ones that the reforms have generated as well as old ones they have failed to resolve.

If this mode of treatment leaves many questions unanswered, at least it serves to dispel numerous misconceptions. Nowhere is this clearer than in the chapter on the health service. The reality that emerges from the heavy cloak in which propagandists have wrapped it will not be recognized by many Americans. Readers unfamiliar with the British scene may also be surprised to learn that the reforms so recently instituted represent no *bouleversement* of traditional practice. Rather they have their origins deep in a past shaped by Liberal and Conservative governments. Examples of this fact recur throughout the book. Labor's program, says Professor Lewis, has roots which "go deeper than World War I; . . . virtually all of its parts at one time or another and in varying degrees have drawn open support from Conservatives and Liberals. It is thoroughly British."

The book makes its main contributions, in this reviewer's judgment, in the introductory chapter on planning and in the brief concluding chapter. The data presented in the first of these chapters and the insights offered in both should prove valuable to student and layman alike. While the remaining chapters deserve commendation for their dispassionate presentation, ample documentation, and restraint in evaluating controversial issues, they are not without inadequacies.



A number of problems fundamental to the postwar reforms receive only cursory attention. Compensation provisions governing payment to former owners of nationalized undertakings are stated, but they are not analyzed nor their alternatives considered. No systematic treatment is given the problems of costing and pricing in publicly owned enterprises. The problems involved in formulating and implementing the investment plans of the public sector are not elucidated. The rationale for divergent administrative arrangements among the nationalized enterprises and, more generally, the whole problem of bureaucracy receive scant mention. The role of the trade unions and the place of industrial democracy under a Labor regime are glossed over. Not least, the book bypasses the problem of productivity which, since the war, has been central to industry and to the economy.

Patently it is too much to expect of any single volume, particularly one which surveys so broad an expanse as *British Planning and Nationalization*, that it will cover satisfactorily all relevant issues. But one may question whether the author has struck a reasonable balance in his emphasis and selection. Too frequently the reader is besieged with details of dubious usefulness. In the discussion of housing, a variety of figures on government subsidies, rents, and building targets are given, but few guides to their understanding and interpretation are provided. In the discussion of rail transport, the reader is exposed to a flood of information on current operations:

Data on wages, costs, revenues, rates, indebtedness, and deficits are enumerated. But there is no framework in which to place these facts, nor are there any criteria by which to appraise them. These are not isolated examples. Such instances will be found in most chapters. Facts and figures serve little purpose unless one has the yardstick that measures their significance.

The book's most serious shortcoming lies perhaps in its failure to elaborate sufficiently the technological, organizational, and human weaknesses that plague the industries and areas it discusses. Just as one cannot judge an answer to a problem unless he is familiar with that problem, so he cannot pass upon Labor's reforms unless he is well acquainted with the weaknesses they were designed to meliorate. The author frequently and justifiably observes that the results of Labor's rule so far are inconclusive and warrant no definitive appraisals. Yet it is not impossible to glean from the record indications as to the basic soundness and probable consequences of Labor's policies. Unfortunately, with the possible exception of the sections on town and country planning, agriculture, and the distribution of industry, the introductory statements of the problem backgrounds are far too brief to give the reader the knowledge sufficient for this task.

The limitations of *British Planning and Nationalization* must be balanced against its virtues. It will serve to inform and enlighten the nonspecialist, while students of the British economy will find it a generally useful reference.

MARVIN FRANKEL